90-407

Supreme Court, U.S.
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No.

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1990

COLLATERAL PROTECTION INSURANCE SERVICES,
CONSOLIDATED FINANCIAL INSURANCE AGENCY,
CONSOLIDATED FINANCIAL INSURANCE AGENCY OF NEVADA,
AND
BARRY MAASHOFF,
Petitioners,

VS.

BALBOA INSURANCE COMPANY,
NEWPORT INSURANCE COMPANY,
NEWPORT MANAGEMENT CORPORATION, AND
INSURANCE AUTOMATION CORPORATION,
Respondents.

On Petition for Writ of Certiorari
to the California Court of Appeal
Third Appellate District

PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED FOR REVIEW

This Petition arises from the affirmance of a state court judgment awarding damages under state law for the reproduction of computer software that is concededly protected by the Copyright Act of 1976 (17 U.S.C. §§ 101 et seq.). This Petition thus presents the following question of federal preemption under 17 U.S.C. § 301(a), a statute never construed by this Court:

> Where computer software is protected from unauthorized copying by the Copyright Act of 1976, does a state court lack jurisdiction to apply state common law to protect against copying of trade secrets because the trade secret remedy is "equivalent" to copyright and therefore expressly preempted under 17 U.S.C. § 301(a)?

PARTIES TO THE PROCEEDING

Your petitioners, defendants below, are: Consolidated Financial Insurance Agency (CFIA), Collateral Protection Insurance Services (CPIS), Consolidated Financial Insurance Agency of Nevada (CFIN) and Barry Maashoff.

Respondents, plaintiffs below, are: Balboa Insurance Company (Balboa), Newport Insurance Company, Newport Management Corporation (NMC or Newport), and Insurance Automation Corporation.

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In The
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October Term, 1990

COLLATERAL PROTECTION INSURANCE SERVICES, CONSOLIDATED FINANCIAL INSURANCE AGENCY, CONSOLIDATED FINANCIAL INSURANCE AGENCY OF NEVADA,
and
BARRY MAASHOFF,
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vs.

BALBOA INSURANCE COMPANY, NEWPORT INSURANCE COMPANY, NEWPORT MANAGEMENT CORPORATION,
and
INSURANCE AUTOMATION CORPORATION,
Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE CALIFORNIA COURT OF APPEAL THIRD APPELLATE DISTRICT

Collateral Protection Insurance Services, Consolidated Financial Insurance Agency, Consolidated Financial Insurance Agency of Nevada, and Barry Maashoff petition for a writ of certiorari to review the judgment of the California Court of Appeal for the Third Appellate District in this case.

OPINIONS BELOW

The official citation to the partially published decision below is *Balboa Ins. Co. v. Trans Global Equities*, 218 Cal.App.3d 1327 (1990). The unofficial citation is *Balboa Ins. Co. v. Trans Global Equities*, 267 Cal.Rptr. 787 (Cal.App. 1990). The opinion is reprinted in the Appendix at p. 1a.

The California Superior Court's Statement of Decision and Judgment were not published, but are reprinted in the Appendix at pp. 60a and 80a.

JURISDICTION

The decision of the California Court of Appeal was filed on March 21, 1990. App. p. 1. Your petitioners' petition for discretionary review to the California Supreme Court was denied on June 7, 1990. App. p. 59a. This Petition is timely, being filed within 90 days thereof. Sup. Ct. R. 13.1.

This Court has jurisdiction to review the judgment below by writ of certiorari under 28 U.S.C. § 1257(a).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

Article I, sec. 8, of the United States Constitution provides congressional power to regulate copyright:

> The Congress shall have Power . . . To promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries.

The Copyright Act preempts "equivalent" state remedies for unauthorized copying under 17 U.S.C. § 301(a):

> (a) On and after January 1, 1978, all legal or equitable rights that are equivalent to any of the exclusive rights within the general scope of copyright as specified by section 106 in works of authorship that are fixed in a tangible medium of expression and come within the subject matter of copyright as specified by section 102 and 103, whether created before or after that date and whether published or unpublished, are governed exclusively by this title. Thereafter, no person is entitled to any such right or equivalent right in any such work under the common law or statutes of any State.

The exclusive rights established by 17 U.S.C. § 106 are as follows:

> Subject to section 107 through 118, the owner of copyright under this title has the exclusive rights to do and to authorize any of the following:
>
> (1) to reproduce the copyrighted work in copies or phonorecords;
>
> (2) to prepare derivative works based upon the copyrighted work;
>
> (3) To distribute copies or phonorecords of the copyrights work to the public by sale or other transfer of ownership, or by rental, lease, or lending;
>
> (4) in the case of literary, musical, dramatic, and choreographic works, pantomimes, and motion pictures

> and other audiovisual works, to perform the copyrights work publicly; and
> (5) in the case of literary, musical, dramatic, and choreographic works, pantomimes, and pictorial, graphic, or sculptural works, including the individual images of a motion picture or other audiovisual work, to display the copyrighted work publicly.

The federal district courts have exclusive jurisdiction over copyright actions under 28 U.S.C. § 1338:

> (a) The district courts shall have original jurisdiction of any civil action arising under any Act of Congress relating to patents, plant variety protection, copyrights and trade-marks. Such jurisdiction shall be exclusive of the courts of the states in patent, plant variety protection and copyright cases.

STATEMENT OF THE CASE

A. Factual Background

Balboa's computer software enhancements, whose reproduction and use by petitioners are the foundation of the judgment below, developed in the following manner.

By January 1981, your petitioners had created, with Balboa's financial assistance, a computerized loan collateral tracking service to ensure the existence of valid insurance for loan collateral. (App. p. 4a.) Petitioners' service used computers to track the insurance status of collateral in which a lender had a security interest, such as an automobile financed by a bank. If the purchaser violated the loan agreement by failing to keep the auto adequately insured, the petitioners' loan tracking service detected this gap in coverage and automatically placed insurance on the vehicle at the purchaser's expense. (App. p. 3a-4a.)

When petitioners were unable to repay their obligations to Balboa, petitioners agreed to give Balboa's affiliate, Newport Management Company (NMC), a perpetual, nonexclusive license to use petitioners' computer software and exclusive ownership of any software enhancement: "Any modification made by NMC shall remain the property of NMC." (App. p. 5a.) NMC hired the software's original developer, Martin Atherton, to make improvements to the software. (App. p. 6a-7a.) Balboa then took over the petitioners' loan tracking center in Stockton, California. (App. p. 6a.)

In exchange for giving the software license and assigning certain lenders to Balboa, petitioners received commissions on the business serviced at the Stockton center. (App. p. 5a.)

Over the next two years, petitioners feared from Balboa's actions and expressed intent that Balboa would destroy petitioners' commission income by transferring all of the Stockton center's business to Balboa's own tracking system in Irvine, California, thereafter selling insurance directly to lending institutions. (App. pp. 7a-8a.)

Accordingly, petitioners established a new tracking center, independent of Balboa, by forming a joint venture with Trans Global Equities, Inc.,[1] by licensing the tracking software (including Balboa's enhancements) to Trans Global, and commencing to service lenders previously serviced at the Balboa center at the new Trans Global center. (App. pp. 8a-9a.)

B. Procedural History

On May 10, 1984 Balboa sued your petitioners for an injunction and damages on account of the use of Balboa's software enhancements, the use of Balboa's confidential information, and the solicitation of Balboa's customers or employees. (App. p. 10a.) In 1984, the trial court gave preliminary relief against Trans Global's use of Balboa's software and confidential information. (App. p. 10a.)

After trial the trial court issued a statement of decision, finding your petitioners responsible for unfair competition in utilizing the software tracking system (including Balboa's enhancements), in soliciting certain lenders, and in hiring certain employees from the Balboa center. (App. p. 69a-70a.)

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[1] An entity not before the Court of Appeal because of bankruptcy proceedings. (App. p. 2a, n.1.)

The trial court found your petitioners liable for unauthorized copying and use of Balboa's computer software:

> Defendants were not authorized by plaintiffs to use or sell plaintiffs' modifications and enhancements or to sell or use the tracking system software with plaintiffs' modifications and enhancements contained in it. Nevertheless, defendants exercised dominion and control over plaintiffs' tracking system software inconsistent with plaintiffs' ownership of said software inconsistent with plaintiffs' ownership of said software by using it in the tracking system of the Trans Global service center. (App. p. 65a.)

The trial court awarded judgment for Balboa against the corporate defendants for $3,871,000 (comprised of $3,721,000 in lost profits and $150,000 in lost profits from sales of the software). (App. 75a.)

On appeal, the corporate defendants sought reversal because the Copyright Act preempted the state law causes of action and vested exclusive jurisdiction in the federal district court. The Court of Appeal allowed your petitioners to raise this contention for the first time on appeal because it raised a question of law addressing a noncurable defect of substance: failure to state a cause of action and lack of subject matter jurisdiction. (App. p. 13a-14a.)

The Court of Appeal ruled that state trade secret remedies were not preempted by the Copyright Act of

1976 and affirmed the judgment.[2] Although recognizing that Balboa's software could have been protected by copyright (App. p. 16a), the Court of Appeal ruled that state laws are not preempted if their violation requires, not just the "mere act of reproduction," but an "extra element" that is "qualitatively different" from copyright infringement. (App. pp. 15a-16a.) On this basis the Court of Appeal held that three state law theories of recovery were not preempted: (1) breach of a confidential relationship; (2) breach of fiduciary duty; and (3) trade secret. (App. pp. 21a-38a.) Only misappropriation was ruled preempted. (App. p. 37a-38a.)

Significantly, the Court of Appeal ruled that California Balboa's software enhancements were protected only by state trade secret law. (App. 43a-44a.) Thus, if this Court rules that in state trade secret law is, in the circumstances of this case, "equivalent" to copyright and therefore preempted, then the judgment must be reversed because the competing Trans Global tracking center could not have been established (and Balboa would not have been damaged) without the copying and use of the software. The other acts found violative of state law--hiring of employees and solicitation of clients--would not have been possible because the Trans Global center could not have functioned without the copying and use of Balboa's software.

The Court of Appeal denied a timely petition for rehearing (App. p. 58a), and the California Supreme Court denied a Petition for Review. (App. p. 59a.)

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[2] With respect to defendant Barry Maashoff, the Court of Appeal reversed the trial court's judgment to impose individual liability upon him for the $3.9 million judgment. (App. pp. 44a-49a; 56a.)

REASONS FOR GRANTING THE WRIT

The Petition should be granted to resolve conflicts in state and federal court rulings on the preemption of state law remedies "equivalent" to copyright under 17 U.S.C. § 301(a), and to settle the important federal question of which state law remedies are "equivalent" to, and therefore preempted by, the Copyright Act of 1976.

This Court has never ruled on the scope of Copyright preemption since Congress enacted the Copyright Act of 1976, preempting state laws that are "equivalent" to copyright. 17 U.S.C. § 301(a).

In the absence of an authoritative pronouncement by this Court, and with the legislative history decidedly unclear on which state remedies are preempted, federal and state courts, as in the instant case, have often given a narrow interpretation to the term "equivalent," readily enforcing state remedies for unauthorized copying. These decisions find state remedies not preempted if they require an "extra element" that is beyond "mere copying" or that may be characterized as "qualitatively different."

These criteria for preemption are both too narrow and too imprecise, allowing state law to erode significantly exclusive federal copyright protection copyright and creating a welter of conflicting federal and state court decisions.

In the instant case, for example, state law protection of Balboa's computer software program may have extended a state remedy where copyright is expressly not available, with respect to "any . . . procedure, process, system, method of operation . . . ." 17 U.S.C. § 102(b). Moreover, by affording relief under state law, the state court permitted Balboa to circumvent the requirement of

registration as a prerequisite to suit and to damages. 17 U.S.C. §§ 411(a), 412.

This Petition should therefore be granted:

1. To prevent state regulation of copyright which, because it is broader than the Copyright Act of 1976,[3] defeats the policy "found in Art. I, § 8, cl. 8 of the Constitution and in the implementing federal statutes, of allowing free access to copy whatever the federal patent and copyright laws leave in the public domain." *Compco Corp. v. Day-Brite Lighting, Inc.*, 376 U.S. 234, 237 (1964).

2. To prevent inconsistent rulings on the preemption of state remedies, rulings that defeat the Congressional goal of a uniform federal system of copyright protection.[4]

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[3] State remedies do not emulate the copyright requirements of proof of authorship, originality and fixation in a proper form. Scott, Computer Law §§ 3.17 to 3.37 (1984). Unlike statutory copyright, state remedies do not require prior registration, they may extend to a "procedure, process, system, method of operation . . . ," 17 U.S.C. § 102(b), their remedy is permanent rather than for the statutory copyright period, 17 U.S.C. § 302(a), and they may entail punitive damages, which are not available in copyright. 17 U.S.C. § 504.

[4] "Instead of a dual system of 'common law copyright' for unpublished works and statutory copyright for published works, . . . the bill adopts **a single system of Federal statutory copyright** from creation . . . . Common law copyright protection for works coming within the statute would be abrogated, and . . . a single Federal system [would be substituted for] the present anachronistic, uncertain, impractical, and highly complicated dual system." H.R.Rep. No. 94--1476, 94th Cong., 2d Sess. 129 (1976)(emphasis added), reprinted in [1976] U.S.Code Cong. & Ad.News 5659, 5745.

I. THE SUBJECTIVE "EXTRA ELEMENT" RATIONALE CREATES CONFLICTING RULINGS ON PREEMPTION, DEMONSTRATING THE NEED FOR THIS COURT'S DETERMINATION OF WHICH STATE REMEDIES ARE "EQUIVALENT" TO COPYRIGHT

A. Congress Expressly Prohibited Enforcement of State Remedies "Equivalent" to Copyright.

The 1976 enactment of 17 U.S.C. § 301(a), prohibiting enforcement of any state remedies "equivalent" to copyright, demonstrated the goal of Congress to eliminate enforcement of state remedies and to create the uniformity of regulation that would inevitably result from the exclusive jurisdiction of federal courts over copyright claims brought under the Copyright Act of 1976.

The legislative history makes manifest the Congressional intent to eliminate the conflicts created by overlapping state and federal remedies. The Report of the House of Representatives states:

> The intention of section 301 is to preempt and abolish any rights under the common law or statutes of a state that are **equivalent to copyright** and that extend to works coming within the scope of the federal copyright law. The declaration of this principle in section 301 is intended to be stated **in the clearest and most unequivocal way possible,** so as to foreclose any possible misinterpretation of its unqualified intention that Congress should act preemptively, and **to avoid the**

development of any vague borderline area as between State and Federal protection.[5]

The enactment of section 301(a), specifically preempting state laws "equivalent" to copyright, substantially altered the requirement for preemption that existed prior to the 1976 Act. Two decisions of this Court while Congress was deliberating on the 1976 Act used the "obstacle" or "conflict" test to uphold state regulation of the subject matter of copyright and patent in the absence of express federal preemption. *Goldstein v. California*, 412 U.S. 546 (1973) (state criminal statute may prohibit copying of recordings for resale where Congress has not spoken on the subject); *Kewanee Oil Company v. Bicron Corporation*, 416 U.S. 470 (1974) (state trade secret law does not conflict with federal protection for patents). These decisions found no preemption because the state laws under review did not "stand[] as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941) (cited in *Goldstein*, 412 U.S. at 561, and in *Kewanee*, 416 U.S. at 479).

The rationale of *Goldstein* and *Kewanee*, however, is not applicable to section 301(a), whose express preemption of state remedies shifted preemption analysis from the search for a conflict between federal and state regulation to the determination whether state remedies are "equivalent" to copyright:

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[5] H.R. Rep. No. 94-1476, 94th Cong., 2d Sess. 130 (1976), reprinted in 1976 U.S. Code Cong. & Ad. News 5659, 5746 (emphasis added).

> "When a federal statute unambiguously precludes certain types of state legislation, we need go no further than the statutory language to determine whether the state statute is preempted." *Aloha Airlines, Inc. v. Director of Taxation*, 464 U.S. 7, 12 (1983).

The legislative history of section 301(a) does not illuminate Congressional intent regarding which state remedies are "equivalent" to copyright. For 13 years the draft version of section 301 listed certain state causes of action (breaches of trust, invasion of privacy, deceptive trade practices such as passing off and false representations--but not trade secret). Prior to enactment, however, this list was deleted "without a satisfactory explanation," leaving the courts to decide which state rights are equivalent to copyright. *Motown Record Corp. v. George A. Hormel & Co.*, 657 F.Supp. 1236, 1239 (C.D. Cal. 1987). *See* Copyright Law Rep. (CCH) § 7305.[6]

This Court has not defined which state remedies are "equivalent" to copyright since section 301(a) was enacted in 1976.

In the absence of a definitive pronouncement by this Court, inferior federal and state courts have struggled to discern the "line between the permissible and the impermissible exercise of state power." *Synercom Technology v. University Computing*, 474 F.Supp. 37, 40-41 (N.D. Tex. 1979). These inferior courts have reached conflicting rulings based upon a

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[6] For a discussion of the legislative history of section 301, see Abrams, Copyright, Misappropriation and Preemption: Constitutional and Statutory Limits of State Law Protection, 1983 Sup. Ct. Rev. 509, 537-548.

variety of rationales that frequently jeopardize the twin Congressional purposes of establishing uniform regulation and prohibiting restrictive state regulation from limiting access to subject matter that would otherwise be in the public domain.

B. The Judgment Below Exemplifies the Lack of an Objective Basis for Determining Which State Remedies are "Equivalent" to Copyright.

The instant case is just the latest example of the conflicting results and confusing rationales generated by inferior courts struggling to determine whether certain state remedies are "equivalent" to state remedies.

Although the court below ruled that state remedies for trade secret and breach of fiduciary duty are not "equivalent" to copyright, the rationale of numerous contrary decisions would, if followed herein, compel reversal of the judgment below.

First, copyright protection for computer software is well-established. 17 U.S.C. §§ 101, 102(a)(1), 117; *e.g., Apple Computer, Inc. v. Franklin Computer Corp.*, 714 F.2d 1240, 1248 (3d Cir. 1983).

Second, copyright protection for computer software has been held, in an analogous case, to preempt state remedies. *Whelan Associates, Inc. v. Jaslow Dental Laboratory*, 609 F.Supp. (E.D. Pa. 1985), *aff'd* 797 F.2d 1222 (3d Cir. 1986), *cert. denied sub nom. Jaslow Dental Laboratory, Inc. v. Whelan Associates, Inc.*, 479 U.S. 1031 (1987).

Whelan Associates had developed for Jaslow a computer software program to aid dental laboratories

in bookkeeping, processing of orders, inventory control, and accounts receivable. Jaslow then created and marketed a derivative program.

For this Jaslow was held liable under the Copyright Act, but state law claims of unfair competition and tortious interference were ruled preempted:

> Plaintiff contends that the use of the name Dentlab constituted a common-law unfair business practice; and that under the common law defendants tortiously interfered with contractual relationships of plaintiff with its customers and tortiously interfered with future prospective contractual relationships . . . . Assuming without deciding that plaintiff has proved such causes of action, no damages have been established that could in any way be quantified or reduced to judgment, beyond those same damages that have been established for the copyright violation. (*Whelan Associates, supra,* 609 F.Supp. at 1323.)

The court below, although assuming that the Copyright Act of 1976 protected Balboa's rights to the computer software (App. p. 16a), nevertheless ruled that state remedies for trade secrets providing the same relief for the copying of computer software were not "equivalent" to copyright and therefore not preempted. (App. pp. 26a-35a.)

The court below first attempted to distinguish the contrary holding of *Videotronics, Inc. v. Bend Electronics*, 564 F.Supp. 1471 (D. Nev. 1983) that the

Copyright Act preempted state trade secret remedies.[7] In ruling that state trade secret law is not preempted, the court below relied upon three decisions that either mistakenly utilized the "obstacle" or "conflict" analysis of *Kewanee* (instead of deciding whether trade secret was "equivalent" to copyright under section 301(a)), *Warrington Assoc. v. Real-Time Engineering Systems*, 522 F.Supp. 367 (N.D.Ill. 1981); *M. Bryce & Assoc. v. Gladstone*, 319 N.W.2d 907 (Wis. App. 1982),[8] or utilized the amorphous "qualitatively different" test. *Brignoli v. Balch Hardy and Scheinman, Inc.*, 645 F.Supp. 1201, 1205 (S.D.N.Y. 1986).

The "qualitatively different" test, often-cited from Prof. Nimmer's treatise, is composed of several illusory and subjective components that the courts have applied neither literally nor consistently. Prof. Nimmer wrote that a right "equivalent to copyright" is one which is infringed "by the mere act of reproduction," whether or not the state right is "broader or narrower than its federal counterpart." On the other handm, "if other elements are required" to invoke the state cause of action "in addition to or instead of, the acts of reproduction, performance, distribution or display," then there is no preemption. 1 Nimmer on Copyright, § 1.01[B] at pp. 1-12 to 1-13 (1990).

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[7] Accord, Avco Corp. v. Precision Air Parts, Inc., 210 U.S.P.Q. (BNA) 894 (M.D.Ala. 1980), aff'd on other grounds, 676 F.2d 494 (11th Cir. 1982).

[8] Accord, S.O.S., Inc. v. Payday, Inc. 886 F.2d 1081, 1089-1090, n.13 (9th Cir. 1989) (citing Kewanee to support conclusion, inter alia, that state trade secret statute is not preempted because it does not "conflict" with copyright.)

As shown below, this formulation has created a welter of conflicting rulings because the determination of what is "qualitatively different" is unavoidably subjective. What is "qualitatively different" rests, like beauty, in the eye of the beholder. Moreover, the "qualitatively different" test does not instruct the court whether it should look for this qualitative difference in the elements of the state cause of action or in the conduct that creates liability. As shown below, the focus of the court's inquiry significantly controls the outcome.

1. Focussing on The Act of Copying Leads To A Finding of Preemption.

Courts that focus on the act of copying universally hold the state law preempted, even though the state law may require something more than "mere copying," and may contain an "extra element" that is "qualitatively different" from copyright. For example, the following state law remedies have been held preempted because--even though their elements may be far removed from copyright--their application rested upon the act of copying.

• Criminal statute barring dealing in stolen property (bootleg tape recordings). *Crow v. Wainwright,* 720 F.2d 1224, 1226 (11th Cir. 1983) (the "prohibited act--wrongfully distributing a copyrighted work--remains the same").

• Interference with contractual relations. *Harper & Row Publishers, Inc. v. Nation Enterprises*, 723 F.2d 195, 201 (2d Cir. 1983), *rev'd on other grounds,* 471 U.S. 539 (1985)("it is the act of unauthorized publication which causes the violation"); *accord,*

Motown Record Corp. v. George A. Hormel & Co. 657 F.Supp. 1236, 1240 (C.D. Cal. 1987); *Maheu v. CBS, Inc.* 201 Cal.App.3d 662, 247 Cal.Rptr. 304 (1988).

• Misappropriation. *Rand McNally & Co. v. Fleet Management Systems*, 591 F.Supp. 726 (N.D. Ill. 1983) (even though state law required an element of "immorality" not a component of copyright); *accord, Ehat v. Tanner*, 780 F.2d 876 (10th Cir. 1985).

• The right of attribution of authorship. *Peckarsky v. American Broadcasting Co., Inc.*, 603 F.Supp. 688, 696 (D.D.C. 1984).

• Injury to reputation. *Ehat v. Tanner*, 780 F.2d 876, 879 (10th Cir. 1986).

• Conversion. *Mayer v. Josiah Wedgewood & Sons, Ltd.*, 601 F.Supp. 1523, 1535 (S.D.N.Y. 1985); *Maheu v. CBS, Inc.*, 201 Cal.App.3d 662, 247 Cal.Rptr. 304 (1988); *Gladstone v. Hillel*, 203 Cal.App.3d 977, 250 Cal.Rptr. 372 (1988)

• Unauthorized assignment of architectural plans. *Robert H. Jacobs v. Westoaks Realtors, Inc.*, 159 Cal.App.3d 637, 205 Cal.Rptr. 637 (1984).

Plainly, if the foregoing decisions had adopted the "extra element" or "qualitatively different" test, they would have reached the opposite result and ruled that the state remedy was not preempted. Conversely, if the court below had focussed on the act of copying Balboa's software rather than on the theoretical elements of the trade secret cause of action, it would have ruled that in the circumstances of this case, the state law remedy for trade secrets was preempted.

2. Comparing Elements of the State Cause of Action to Copyright Leads to Conflicting Rulings.

When courts shift their focus from the act of copying to the elements of the state cause of action and ask (as did the court below) whether the state cause of action contains an "extra element" or is "qualitatively different," rulings on preemption are in conflict because of the subjective nature of these standards. For example, courts have reached opposite conclusions regarding the copyright preemption of the following state law remedies.

• Breach of fiduciary duty. One court ruled that this state law claim did not add an "extra element" and was therefore preempted, *Del Madera Properties v. Rhodes and Gardner, Inc.*, 820 F.2d 973 (9th Cir. 1987). Other courts have found that a breach of fiduciary duty is "different in kind" from copyright and therefore not preempted. *Oddo v. Ries*, 743 F.2d 630, 635 (9th Cir. 1984); *Ronald Litoff, Ltd. v. American Express Co.*, 621 F.Supp. 981, 986 (S.D.N.Y. 1985); *P.I.T.S. Films v. Laconis*, 588 F.Supp. 1383, 1386 (E.D.Mich. 1984).

• Unjust enrichment. Two courts have held that this state law claim is preempted *Del Madera Properties v. Rhodes and Gardner, Inc.*, 820 F.2d 973 (9th Cir. 1987) (implied promise not to use or copy materials "is equivalent" to copyright); *Ronald Litoff, Ltd. v. American Express Co.*, 621 F.Supp. 981, 986 (S.D.N.Y. 1985). A third court reached the opposite conclusion. *Schuchart & Assoc., etc. v. Solo Serve Corp.*, 540 F.Supp. 928, 944-945 (W.D.Tex 1982) (promise to pay for services is "not equivalent.")

• Trade secret. As noted, one court has ruled that this state remedy is preempted by copyright, *Videotronics, Inc. v. Bend Electronics*, 564 F.Supp. 1471, 1477, but another court, cited by the court below, utilized the amorphous "qualitatively different" test to rule state trade secret law not preempted. *Brignoli v. Balch Hardy and Scheinman, Inc.* 645 F.Supp. 1201, 1205 (S.D.N.Y. 1986).[9]

Such conflicting decisions--the inevitable result of the subjective nature of the "extra element" and "qualitatively different" standards--jeopardize the uniformity sought by Congress in requiring exclusive federal copyright jurisdiction and threaten the constitutional policy promoting free access to intellectual property.

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[9] The other two decisions cited by the court below utilize the "obstacle" or "conflict" analysis of Kewanee, which is clearly inappropriate in light of the express preemption of "equivalent" remedies in section 301(a), further demonstrating the need for a clarifying decision by this Court. Warrington Assoc. v. Real-Time Engineering Systems, 522 F.Supp. 367 (N.D. Ill. 1981); M. Bryce & Assoc. v. Gladstone, 319 N.W.2d 907 (Wis. App. 1982).

CONCLUSION

The threat to exclusive federal jurisdiction over copyright and the lack of uniformity created by the conflicting interpretations of "equivalent" state remedies needs to be dispelled by a decision of this Court. Lower courts should be directed to focus the preemption inquiry on the act of copying. If the application of the state remedy is triggered by the act of copying, that remedy is equivalent to copyright and therefore preempted.

The petition for a writ of certiorari should therefore be granted to announce this criterion for determining the preemptive effective of 17 U.S.C. § 301(a).

Respectfully submitted,

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CERTIFIED FOR PARTIAL PUBLICATION*

COURT OF APPEAL OF THE STATE OF CALIFORNIA

THIRD APPELLATE DISTRICT

BALBOA INSURANCE CO., et al.,

Plaintiffs, Respondents and Cross-Appellants,

v.

TRANS GLOBAL EQUITIES, et al.,

Defendants, Appellants and Cross-Respondent

3 Civil C000793

APPEAL from the Judgment of the Superior Court
Of San Joaquin County, Frank Kim, Judge
Affirmed in Part, Reversed in Part

OPINION FILED March 21, 1990

Defendants Trans Global Equities (Trans Global), Collateral Protection Insurance Services (CPIS), Consolidated Financial Insurance Agency (CFIA) and Consolidated Financial Insurance Agency of Nevada (CFIN), appeal from the judgment for plaintiffs Balboa Insurance Company (Balboa), Newport Insurance Company, New-

* Pursuant to California Rules of Court, rule 976.1, the Reporter of Decisions is directed to publish all of this opinion except Parts II, III, and IV.

port Management Corporation (NMC or Newport), and Insurance Automation Corporation.[1] The court awarded Balboa $3,721,000 as profits lost from the defendants' unfair competition with Balboa's insurance businesses. The court also awarded Balboa $75,000 in profits lost when three of the defendants sold Balboa's computer software enhancements.[2] Balboa cross-appeals from the portions of the judgment in favor of Barry Maashoff.[3]

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[1] For convenience, unless otherwise indicated, we refer to the respondents collectively as "Balboa" and the appellants simply as "defendants." All of the respondents appear to be part of a larger whole occasionally identified in the record as "Avco" or "Avco Financial Insurance Group."

In addition to Trans Global Equities, the judgment named as defendants: "Trans Global in whatever form or name it may exist, except Trans Global Equities, Inc." The judgment lists 15 different entities bearing Trans Global's moniker. For convenience, unless otherwise indicated, we refer to the Trans Global entities collectively as "Trans Global."

Since Trans Global Equities, Inc. had filed for bankruptcy, the court severed Balboa's claims against it and reserved jurisdiction. Accordingly, that entity is not before this court.

[2] The court's statement of decision gave Balboa $150,000 for the lost software sale profits. The judgment itself, however, awarded only $75,000. Neither party asks us either to resolve the apparent conflict or interpret that portion of the award.

[3] The court gave judgment to each of the eight individuals Balboa sued. In its notice of cross-appeal, Balboa challenged the judgment as to four of those eight. In its briefs here, however, it only seeks reversal of the judgment in favor of Barry Maashoff. Accordingly, we deem abandoned any challenge to the judgment favoring any of the other individual defendants.

For convenience, unless otherwise indicated or required by context, all references to appellants as "defendants" also include cross-respondent Maashoff.

In the published part of the opinion, we address the impact of federal copyright law upon California law regarding unfair competition. To the extent that unfair competition claims rest on trade secret and breach of confidential or fiduciary relationships, they survive a preemption challenge. In the unpublished parts of the opinion we find substantial evidence of breached duties of fidelity and confidentiality, we uphold the trial court's appointment of an expert and calculation of damages, and in considering Balboa's cross-appeal, we shall reverse the trial court's judgment in favor of defendant Barry Maashoff.

BACKGROUND

Collateral protection insurance covers a lender's interest in the property that secures a loan. Under typical loan agreements, if the borrower fails to insure the collateral for physical damage, the lender may purchase a policy insuring its security interest and charge the premiums to the borrower.[4]

In 1972, Jack Nelson began a loan collateral tracking service in Stockton. He formed the company eventually known as "Collateral Protection Insurance Services" (CPIS) to help banks and credit unions keep track of their collateral's insurance status.[5] As insurance agents, Nelson

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[4] Insurers use two interchangeable terms, "Lender's Single Interest (LSI)" and "Vendor's Single Interest (VSI)," to denominate such policies. Lenders pay the policy premiums and then add the premiums to a loan's balance.

[5] CPIS is synonymous with "Collateral Protection Insurance" (CPI).

and company could then sell insurance for any uninsured collateral.

The laborious business of tracking thousands of loans on three-by-five index cards lent itself readily to computerization. By 1979, CPIS had hired programmer Martin Atherton to design software for a Hewlett-Packard computer. That same year, insurance agent Barry Maashoff joined CPIS as its president and manager of the Stockton tracking center. Also that year, to finance the Atherton system, CPIS borrowed $500,000 from Balboa Insurance Company. At the same time, CPIS agreed to sell Balboa's collateral insurance policies to its tracking customers.

By June 1980, CPIS and its agents owed Balboa "several hundred dollars" in premiums for collateral insurance policies placed with Balboa for various lenders. Although CPIS had collected the money from its lenders, it had diverted the funds owed Balboa to "[o]ther purposes and other uses than remitting to Balboa[.]"

To resolve this "out of trust" situation, in June 1980, Balboa required Nelson, Maashoff and other CPIS investors to sign personal guarantees for $1 million. In addition, Balboa required CPIS and its principals to secure the guarantees with the computer tracking system. Finally, Balboa required the new joint venturers of the restructured Stockton Service Center to write all their business with Balboa.[6]

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[6] In June 1980, CPIS and two other insurance companies formed two new entities as joint ventures: Consolidated Service Bureau (CSB) and Consolidated Financial Insurance Agency (CFIA). CSB ran the Stockton tracking center. Maashoff continued to head the center's operations during CSB's tenure. For its part, CFIA contracted to

In January 1981, Nelson or Maashoff told Balboa that CPIS and its principals could not make even interest payments on the outstanding debt. As a result, Balboa, CPIS and the joint venturers negotiated four agreements signed in March 1981. At trial, the parties submitted these agreements as joint exhibits and refer to them here by their exhibit numbers. For convenience, we adopt their nomenclature.

In Exhibit 1(a), CPIS gave Balboa's affiliate, Newport Management Company (NMC), a perpetual, nonexclusive license to use the computer tracking software.[7] As part of the license, CPIS authorized NMC to modify the software as NMC saw fit. CPIS agreed that "[a]ny modification made by NMC shall remain the property of NMC."

In exchange for the license, NMC agreed to pay CPIS "special override" commissions. Memorialized in Exhibit 1(b), this commission agreement applied to business written on 20 accounts listed on "Exhibit A" attached to the override agreement. NMC agreed to pay CPIS between 1 and 5 percent of net insurance premiums received from Exhibit A policies.[8]

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write policies for Balboa. CFIA's joint venturers agreed to transfer all of their collateral protection clients' business to Balboa.

[7] NMC forms part of Balboa's group of companies.

[8] The percentage changed as the "combined annual loss ratio produced by such policies" increased. For loss ratios 50 percent or less, NMC promised to pay a full 5 percent commission. The commission dropped 1 percent for each percent the loss ratio increased until it reached its 1 percent floor for loss ratios of 55 percent or over.

In Exhibit 1(c), Balboa released Nelson from his obligations as one of CPIS' guarantors. In exchange, he agreed not to cause any of the 20 accounts listed in Exhibit A or any of an additional 92 accounts listed on an attached Exhibit B to cancel or lapse for six months.

Finally, in Exhibit 1(d), CPIS agreed to transfer to Balboa its rights to normal commissions from the Exhibit A accounts. CPIS also promised "that it will take no action to cause such policies of insurance to be canceled, lapse or otherwise terminate." In exchange, Balboa agreed to pay CPIS a 5 percent servicing override commission and to release CPIS from its obligations under the 1980 $1,000,000 note and security agreement.

In Exhibit 1(d), Balboa also agreed to pay a similar 5 percent commission for three years on the 92 Exhibit B accounts. In March 1984, however, the commissions dropped to 1 percent and expired completely five years later. CFIA also signed this agreement.

Shortly after the parties negotiated the four agreements, NMC took over the Stockton loan tracking center's operations. NMC hired Maashoff as its employee to manage the center. Maashoff headed the Stockton Service Center until September 1981. At that time, he left Balboa's employment to concentrate on selling collateral protection insurance nationwide. In mid-December 1982, Maashoff returned as a "management consultant" to direct the Stockton center's attempts to run more efficiently and smoothly.

After it took over the Stockton center's operations, NMC continued to improve the software licensed from CPIS. It hired the software's original developer, Martin

Atherton, to make some of these enhancements. Balboa's employees made others. Maashoff was involved in many of the changes. By 1983, the system's improvements and other changes allowed the Stockton center to become profitable for the first time.

NMC's assumption of management duties at the Stockton center and the transfer of the Exhibit A accounts to Balboa reduced CPIS to collecting its service commissions and marketing its software to other potential loan tracking services. Unfortunately for CPIS, when it licensed its software to NMC in March 1981, both CPIS and Atherton had neglected to keep a copy of the base system.

In 1983, CPIS licensed its software to American Bankers for $150,000. To reconstruct the March 1981 base system, Atherton used a copy of Balboa's system as of September 1981. The September 1981 tape, however, contained extensive changes made by Balboa to the base system. Despite Atherton's efforts to delete these enhancements, the copy of the system delivered in May 1983 to American Bankers contained some. After discussions with Balboa, Atherton attempted again to remove all of Balboa's program material. Even after delivery of the amended tape in late 1983, at least one of Balboa's programs remained in the American Bankers system.

By late 1983, while still the "management consultant" streamlining NMC's Stockton center operations, Maashoff began preparations to form a competing insurance tracking service. He feared that Balboa was going to transfer all of the Stockton center's business to its own system in Irvine. In addition, he feared that Balboa was going to sell insurance directly to the lending institutions. He felt that Balboa would use these actions to reduce or eliminate

commissions that CPIS and CFIA might otherwise earn.[9] Accordingly, in January 1984, CPIS and Trans Global formed a joint venture to establish the Trans Global Financial Service Center in Stockton.

That same month, CPIS licensed its tracking software to Trans Global. On January 30, 1984, Trans Global hired Maashoff to manage the Trans Global center.[10] He began planning for the new center's building and equipment. He also planned the center's personnel requirements. As part of his efforts to staff the new center, Maashoff discussed the strengths and weaknesses of Balboa's employees with Jan Mehlhaff, a department supervisor at Balboa's Stockton Service Center. Maashoff also began to plan to move accounts from Balboa's tracking service to the new Trans Global center. Fearing that Balboa might find some way to stop it, Maashoff, CPIS, and Trans Global kept their plans secret from Balboa.

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[9] As noted above, however, under Exhibit 1(d), many of the commissions were scheduled for reduction from 5 to 1 percent on March 1, 1984. Moreover, in an amendment to Exhibit 1(d), Balboa had agreed to pay CPI for three years a 5 percent override commission on all accounts "produced directly by the influence of CPI or CFIA" that Balboa transferred from Stockton to Irvine. After March 31, 1984, Balboa agreed to pay a 1 percent commission on such accounts for an additional five years.

[10] Trans Global contracted with CPIS to CPIS' "agent and employee," Maashoff, run the new center. The agreement specifically gave Maashoff the right to continue "supervising the operation of [NMC] servicing center ... and making required changes to programs licensed to [NMC]."

During April and May of 1984, events came to a head. In early April, Maashoff met with Balboa's head, Jack Trapp, to propose a deal. Maashoff told Trapp that Balboa could service in its Irvine center any accounts it wanted and that Trans Global would service the rest in its new Stockton center for a commission. A few days later, before he could respond definitively, Trapp resigned as Balboa's president.

Trans Global then moved forward in its plans to compete with Balboa. Trans Global arranged to sell collateral protection insurance from two other carriers. Nelson and Maashoff had a phone line for Trans Global installed in Balboa's Stockton tracking center.

In late April and early May, Nelson solicited for Trans Global and the new carriers some of the Exhibit A accounts that CPIS had assigned to Balboa in 1981. Maashoff felt that they were just taking back these "customers that belonged to [us.]" Many came over. Trans Global promised these customers that the transfer from Balboa to Trans Global meant only a telephone number change; the tracking system, personnel, even the mailbox, would remain the same.

In April, Maashoff announced the Trans Global center's opening to Balboa's employees. He hoped "to solidify a loyal base of employees for Trans Global in the event that [Balboa] refused to follow [Maashoff's] proposal [to take over Balboa's accounts] . . . ." He directly approached department supervisors Melhaff and Fenley as well as employee Jodie Thomas. He successfully lured Melhaff. He told other key Balboa employees of the availability of jobs with Trans Global.

In early May, Maashoff had one of Balboa's programmers, Susan McCrory, spend two weeks of her vacation working at Trans Global's new center. Maashoff had her complete programs she had been writing for Balboa so that both Trans Global and Balboa could use them.[11]

The developments' pace continued to accelerate in early May. At that time, Maashoff learned that Balboa was going to close the Stockton center and transfer the business to its Irvine system. Maashoff encourage Balboa supervisor Darryl Fenley to organize a walkout of Balboa's remaining employees.[12] Maashoff also urged Balboa's employees to forward tapes containing certain client information from Balboa to Trans Global without notifying Balboa immediately that the clients were leaving.

On May 10, 1984, Balboa sued for an injunction and damages against Trans Global. Among other things, its complaint asked the Court to enjoin Trans Global from: 1) using or transferring Balboa's enhancements to the "support system and software;" 2) "using ... any confidential information obtained from [Balboa];" and 3) soliciting Balboa's customers, agents, or employees. In late May and early June, the Court granted preliminary relief against Trans Global's use of Balboa's software and confidential information.

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[11] At her deposition, McCrory testified that these programs were as much as 95 percent complete at the time she brought them down to Trans Global to finish. Maashoff disputed her estimate.

[12] Balboa announced the closure, effective May 18, on May 4. Fenley did not organize a walkout.

Trans Global then answered and cross-complained for breach of contract, breach of the covenant of good faith and fair dealing, and abuse of process. The Court sustained with leave to amend Balboa's demurrer to the abuse of process and breach of contract claims. Upon Trans Global's failure to amend timely, the Court dismissed these two cause of action. Balboa eventually dismissed its "breached good faith covenant" claim, raising the argument solely as an affirmative defense.

On July 31, 1984, each side deposited in court a copy of their computer software source codes. They stipulated that such software was "valuable and confidential trade secrets which are the essence of the competitive advantage of their respective businesses" and agreed to limit disclosure only to litigations needs.

Trial eventually began April 16, 1985. The court trial extended over 23 days. The evidence conflicted substantially.

Following trial, on July 5, 1985, the Court appointed Larry Dold to analyze the testimony and exhibits regarding the software copying. Dold outlined his conclusions in a letter to the Court. The parties later examined him at a hearing on the report.

In his letter, Dold concluded that: "1. Many of the fixes, or corrections of errors, implemented by Balboa after March 19881 remain in the Trans Global program. 2. l Some of the enhancements and changes made by Balboa after March 1981 are still in the Trans Global programs. 3. Trans Global requested Susan McCrory to not only come to work for them during 1984, but to also

bring with her copies of programs that she was currently working on at Balboa."

At the hearing, he amplified his conclusions. He noted that the bare number of program lines did not necessarily reveal a given modification's importance. He also doubted strongly that Atherton's memory could account for the extent of duplication between the systems. He also testified that Atherton could only have independently recreated the extensive modifications with great difficulty.

The Court issued its intended decision on December 11, 1985. The Court announced its intent to find that the Complaint stated one cause of action, for unfair competition.[13] The Court tentatively found that Trans Global and the other defendants competed unfairly in three ways: 1) by soliciting the Exhibit A accounts; 2) by hiring away Balboa's key employees; and 3) by selling and using Balboa's software modifications without authorization. The Court rejected the defendants' affirmative defenses.[14] It tentatively awarded Balboa $3,721,000 as lost profits and $150,000 for the unauthorized sale of the Balboa software modifications.

The Court issued its statement of decision on July 18, 1986. In addition to the three unfair competition grounds

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[13] The court rejected Balboa's claim that the complaint stated four separate causes of action. In addition to the unfair competition claim, Balboa had argued that its complaint stated claims for breach of contract, conversion and breach of the covenant of good faith and fair dealing.

[14] Neither the tentative decision nor the statement of decision mention the "breach of the covenant of good faith and fair dealing" defense.

tentatively found, the Court also concluded that the defendants competed unfairly when they "utilized the managerial efforts of Barry Maashoff to create a competing loan tracking service for Trans Global." The Court left intact its damages calculation. The Court refused to find either Maashoff or Nelson liable individually. On July 22, 1986, the Court entered judgment and these timely appeals followed.

DISCUSSION

I. COPYRIGHT LAW DOES NOT PREEMPT UNFAIR COMPETITION CLAIMS BASED ON TRADE SECRET AND BREACHES OF CONFIDENCE OR FIDUCIARY DUTY.

A. DEFENDANTS MAY RAISE THEIR PREEMPTION ARGUMENT.

Defendants contend that federal copyright law preempts Balboa's unfair competition claim. They admit they did not raise this defense below. Nevertheless, they claim that the copyright preemption defense goes to the trial court's jurisdiction. We agree.

As Balboa notes, normally we do not consider affirmative defenses not tendered below. (See, e.g. *Royster v. Montanez* (1982) 134 Cal.App.3d 362, 366.) Nevertheless, as Witkin notes, exceptions exist. "The rule that the appellate court will not consider points not raised below ... is limited to matters involving only the rights and interests of the litigant which could have been cured in the trial court. It does not apply to the following: (1) A noncurable defect of substance where the question is one of law, such

as lack of jurisdiction ... or complete failure to state a cause of action...." (9 Witkin, Cal. Procedure (3d ed. 1985) Appeal, § 315, p. 326, emphasis added.)

Here, both of the above-mentioned exceptions apply. First, to the extent defendants establish preemption, by definition no state cause of action exists. Second, federal law gives exclusive jurisdiction over copyright disputes to the federal courts. (28 U.S.C.S. § 1338(a).) A successful copyright preemption argument would eliminate the trial court's very power to enter judgment over the defendants here. Accordingly, we shall consider the preemption argument.[15]

B. COPYRIGHT LAW DOES NOT PREEMPT UNFAIR COMPETITION CLAIMS BASED ON TRADE SECRET AND BREACHES OF CONFIDENCE OR FIDUCIARY DUTY.

Federal law expressly preempts state laws that aim to protect "legal or equitable rights that are equivalent to any of the exclusive rights within the general scope of copyright as specified in [17 U.S.C.S. § 106.... [After January 1, 1978] no person is entitled to any such right or equivalent right in any such work under the common law or statutes of any State." (17 U.S.C.S. § 301(a).) (Further citations to undesignated code sections refer to this Title.) At the same time, federal law allows states to regulate

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[15] (Accord Boeing v. Sierracin (Wash. 1987) 738 P.2d 665, 674 [since preemption goes to court's jurisdiction, appellate court will consider it]; see contra J & K Computer Systems, Inc. v. Parrish (Utah 1982) 642 P.2d 732, 736 [failure to raise preemption as affirmative defense in trial court bars consideration on appeal].)

"activities violating legal or equitable rights that are not equivalent to any of the exclusive rights within the general scope of copyright as specified by [17 U.S.C.S. § 106]." (17 U.S.C.S. § 301(b)(3).) Moreover, the statute that gives the federal courts exclusive jurisdiction over copyright claims allows jurisdiction over state law "unfair competition" claims when joined with a substantial and related claim under copyright laws. (28 U.S.C.S. § 1338(b).) Thus, copyright's preemptive effect on a state unfair competition claim depends upon whether the state law protects "legal or equitable rights that are equivalent" to the exclusive rights specified in section 106.

Section 106 generally gives a copyright owner exclusive right: "(1) to reproduce the copyrighted work ...; (2) to prepare derivative works based upon the copyrighted work; (3) to distribute copies ... of the copyrighted work to the public by sale or other transfer of ownership, or by rental, lease, or lending; (4) [if applicable] to perform the copyrighted works publicly; and (5) [if applicable] to display the copyrighted work publicly." (17 U.S.C.S. § 106.) Borrowing section 106's language, Professor Nimmer summarizes: "a right which is 'equivalent to copyright' is one which is infringed by the mere act of reproduction, performance, distribution or display." (1 Nimmer on Copyright (Rel. 23) § 1.01[B], at p. 1-12 [footnotes deleted; hereinafter, "Nimmer"].)

Nimmer elaborates: "If under state law the act of reproduction, performance, distribution or display, no matter whether the law includes all such acts or only some, will in itself infringe the state created right, then such right is preempted. But if other elements are required, in addition to or instead of, the acts of reproduction, performance, distribution or display, in order to constitute a state

created cause of action, then the right does not lie 'within the general scope of copyright,' and there is no preemption." (Id. at p. 1-13 [emphasis in original, footnotes deleted].)

Courts have denominated Nimmer's analysis the "'extra element' test." (See, e.g., Gladstone v. Hillel (1988) 203 Cal.App.3d 977, 987.) "While generally accepting this test, the courts have demanded that the extra element 'must be one that changes the nature of the action so that it is qualitatively different from a copyright infringement claim.' [Citations, emphasis in source of quotation]." (Ibid.)

We assume strictly arguendo that Balboa could have received copyright protection for its software modifications. (See, e.g., Whelan Associates, Inc. v. Jaslow Dental Laboratory (3d Cir. 1986) 797 F.2d 1222, 1229-1242, Apple Computer, Inc. v. Franklin Computer Corp. (3rd Cir. 1983) 714 F.2d 1240, 1248.)[16] Copyright law would thus have protected Balboa from unauthorized duplication or transfer of its programs by Maashoff, Atherton or CPIS. To survive preemption, Balboa's complaint must allege an element beyond "unauthorized duplication or transfer." Moreover, that element must make the state claim

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[16] The record does not allow us to determine the scope, if any, of such copyright protection. In general, a copyright applicant must demonstrate authorship, originality and fixation in a proper form. (See generally Scott, Computer Law (1984) §§ 3.17 to 3.37.)

Plaintiffs' failure to comply with such statutory prerequisites to copyright protection as notice or deposit does not allow them to evade any of copyright's preemptive sweep. (See 1 Nimmer, supra, § 1.01[B]; Maheu v. CBS, Inc. (1988) 201 Cal.App.3d 662, 672.)

"qualitatively different from a copyright infringement claim."

We turn first to the complaint itself. After a 23-day trial, the court below concluded that the complaint stated only a cause of action for "unfair competition."[17] Admittedly, the defendants' failure to raise its defense below prevented the trial court from analyzing the complaint under copyright preemption law. Nevertheless, two reasons made the court's use of the unfair competition label unfortunate.

First, it merely begs the preemption question: does copyright preempt these kinds of unfairly competitive acts merely because they involve computer software? "Unfair competition" includes a broad range of claims. At best, copyright preempts only some of the claims included in the term "unfair competition". (See, eg., Smith v. Weinsten (S.D.N.Y. 1984) 578 F. Supp. 1297, 1306-1308 [unfair competition preempted only to extent that plaintiffs seek to recover profits defendant derived from unauthorized use of ideas; "palming off" branch of unfair competition law not preempted; breach of confidence not preempted]; see also Walker v. Time Life Films (2d Cir. 1986) 784 F.2d 44, 53 [unfair competition preempted to extent plaintiff seeks

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[17] Balboa's complaint make no attempt to identify its theories of relief. Defendants did not demurrer or otherwise attempt to get Balboa to state its theories of relief specifically. The parties appear to have framed the case below simply by reference to general equitable principles.

As such, the parties virtually ignored the specific elements of unfair competition claims for breach of confidence, breach of fiduciary duty and trade secret misappropriation. This failure to frame the pleadings and trial in conventional legal terms has greatly and unnecessarily complicated our review of this 3000-page record.

protection against copying; breach of confidence not preempted].)

The breadth and analytical vagueness of unfair competition law complicates the preemption analysis greatly. One branch of unfair competition law involves contractual provisions by one party, usually an employee or partner, not to compete against its former employer or partner. (See, e.g., Bus. & Prof. Code §§ 16600-16602; The Law of Competitive Business Practices (Cont.Ed.Bar. 1981) pp. 60-64.) Courts usually construe these covenants narrowly against the former employer or partner. (See, e.g., KGB, Inc. v. Giannoulas (1980) 104 Cal.App.3d 844, 847-855.) Although defendants here cite many of these competitive restraint cases, no such express covenants apply to this case's resolution.

Beyond the contractual branch lies a host of often overlapping theories in the tort branch. "[I]n addition to valid contractual provisions [not to compete unfairly], an employer may use one or more tort theories to support an injunction against unfair competitive activities by a former employee: breach of confidential relationship, breach of fiduciary duty, interference with prospective economic advantage, advantageous business relationship [sic], and interference with contractual relations." (The Law of Competitive Business Practices, supra, at p. 63.) Each of these tort theories raises its own issues. As demonstrated more fully below, the complaint arguably implicates at least two of these tort theories.

Two other branches of unfair competition also arguably apply. Courts and commentators frequently analyze separately unfair competition and trade secrets protection. (See id. at p. 109 [law of trade secrets "can augment the

traditional business torts of unfair competition...and breach of fiduciary duty...."]; see also post, footnotes 19-22 and accompanying text.) Nevertheless, at bottom, trade secret protection is itself but a branch of unfair competition law. (See, e.g., *KGB, Inc.*, supra, 104 Cal.App.3d at p. 850; Comment, Simultaneous Copyright and Trade Secret Protection for Computer Programs (1983) 23 Santa Clara L. Rev. 1037, 1039 ["Trade secrecy is a branch of unfair competition...."]; Scott, Computer Law (1984) § 5.30, at pp. 5-27, 5-28 [hereinafter, "Scott"].)

Common law misappropriation presents a final legal theory under the broad unfair competition umbrella. The doctrine originated in the United States Supreme Court's decision of International News Service v. Associated Press (1918) 248 U.S. 215. (See Scott, supra, at p. 5-28.) "It is normally invoked in an effort to protect something of value that is not covered either by patent or copyright law on the one hand, or by traditional doctrines of unfair competition, such as trade secret theft or breach of confidential relationship, on the other." (Id. at pp. 5-27 to 5-28 [footnotes deleted].) The cause of action has three elements: "(1) the plaintiff has invested substantial time and money in development of its ...'property'; (2) the defendant has appropriated the [property] at little or no cost; and (3) the plaintiff has been injured by the defendant's conduct." (Id. at p. 5-28.)

In addition to common law unfair competition, California has a statute allowing a court to enjoin unfairly competitive acts. (See Bus. & Prof. Code, §§ 17200 & 17203.) The remedies available under the statute are "cumulative to each other and to the remedies or penalties available under all other laws of this state." (Bus. & Prof. Code, § 17205.) Plaintiffs have not argued here or below

that they seek relief under this statute. Accordingly, it appears they have confined their claim to common law unfair competition. For a second reason, the trial court's use of the unfair competition label is unfortunate. In a proper case, the same conduct may support relief under multiple theories.[18] Preemption law, however, requires analysis of each theory to determine whether it contains the necessary qualitatively different extra element distinguishing it from copyright protection. Indeed, courts and commentators have devoted considerable attention to the preemptive effect of copyright on trade secret alone.[19] Accordingly, in reviewing plaintiffs' complaint, we must consider the range of potential theories of unfair compe-

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[18] For example, a trade secrets claim often requires proof of a confidential relationship. (See, e.g., Rest. (First) Torts, § 757(b) & comm. (j).) The relationship of principal and agent exemplifies such confidential relationships. (Id. at comm. (j), p. 13.) An agent, however, owes duties of loyalty and confidence independent of information's "trade secret" status. (See, e.g., Rest.2d Agency, §§ 387 & 956.) Thus, the same conduct conceivably could give rise to three claims: 1) improper use or disclosure of trade secrets; 2) breach of the duty of confidence; and 3) breach of fiduciary duty.

[19] (See, e.g., Bender, Protection of Computer Programs: The Copyright/Trade Secret Interface (1986) 47 U. Pitt. L. Rev. 907 [hereinafter, "Bender"]; Hazen, Contract Principles as a Guide for Protecting Intellectual Property Rights in Computer Software: The Limits of Copyright Protection, the Evolving Concept of Derivative Works, and the Proper Limits of Licensing Arrangements (1986) 20 U.C. Davis L. Rev. 105; Comment, Federal Copyright Protection and State Trade Secret Protection; The Case for Partial Preemption (1984) 33 Am U.L. Rev. 667; Rosen, A Common Law for the Ages of Intellectual Property (1984) 38 U. Miami L. Rev. 769; Comment, Problems of Interpretation under the 1980 Computer Amendment (1983) 23 Santa Clara L. Rev. 1001; Comment, Simultaneous Copyright and Trade Secret Protection for Computer Programs (1983) 23 Santa Clara L. Rev. 1037.)

tition. Similarly, in reviewing the case law covering the range of unfair competition claims, we must separate the particular theories confronting each court.

Construction of a complaint presents a legal question for our independent review. "As a reviewing court we are not bound by the construction placed by the trial court on the pleadings but must make our own independent judgment thereon, even as to matters not expressly ruled upon by the trial court." (Miller v. Bakersfield News-Bulletin (1975) 44 Cal.App.3d 899, 901.)

The critical portions of the complaint come in paragraphs 7 through 13. In those paragraphs, Balboa outlines its claims involving its alleged confidential relationship with Maashoff. The allegations first focus on Maashoff's "access to confidential information regarding all aspects of the business of [Balboa]...." Balboa then gave four examples of Maashoff's "access to confidential information regarding all aspects of the business of [Balboa]...." Balboa then gave four examples of Maashoff's knowledge of confidential information: 1) "the content, capabilities, and operation of the updated support system and computer software developed by plaintiffs since acquisition of the system March 4, 1981"; 2) "the commission structure for the agents writing insurance with Balboa ..."; 3) "the terms and conditions of employment of Newport's Stockton employees"; and 4) "the identity and other information concerning clients and accounts...."

The complaint then alleges that Maashoff and the other defendants used the confidential information and "have induced agents and lending institution accounts writing insurance with Balboa through Newport as a general agent to transfer business to Trans Global and are

attempting to prevail upon other agents to do the same; defendants induced employees of Newport to terminate employment with Newport and to undertake employment with Trans Global and have threatened to induce all of Newport's employees to leave Newport for Trans Global."

These portions of the complaint reveal Balboa's principal claimed right and the effect of the defendants' alleged wrong. First, Balboa claims a right in certain confidential information essential to its business. The computer software plays only one of four specified parts of the overall essential information. Indeed, the software itself is identified in tandem with "the updated support system." The complaint's face thus further narrows the software's importance by distinguishing the support system in general and the software in particular.

Second, the harm allegedly done to Balboa comes from the use of this confidential information to lure Balboa's clients and employees and render valueless the consideration CPIS paid to Balboa in 1981. In these portions of the complaint, Balboa does not allege an improper "reproduction, performance, distribution or display." Rather, in effect, Balboa alleges that the knowledge gained from the confidential information allowed defendants an improper head start in its competition with Balboa.

We construe the complaint liberally. In such light, the above portions of the complaint outline claims arguably arising under four unfair competition theories:

breach of confidential relationship,[20]

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[20] The Restatement Second of Agency generally describes an agent's duties to maintain a principal's confidences. (Rest.2d Agency, §§ 395 & 396.) Section 395 states: "Unless otherwise agreed, an agent is subject to a duty to the principal not to use or to communicate information confidentially given him by the principal or acquired by him during the course of or on account of his agency or in violation of his duties as agent, in competition with or to the injury of the principal, on his own account or on behalf of another, although such information does not elate to the transaction in which he is then employed, unless the information is a matter of general knowledge." Section 396 then extends the duty even after the agency's termination "unless otherwise agreed."

The defendants argue that Maashoff owed no such duties since the complaint describes him as a "consultant." We consider below the evidence critical to this question's determination. Here, however, we focus solely on the pleadings. The complaint adequately alleges that Newport "employed" Maashoff. Normally, an "employee" owes a duty to preserve the employer's confidences. (See, e.g., id. at §2(2) & com. a-d, § 396(b) & com. b.)

In addition to the specific duties of confidence owed by an agent, several California courts have recognized an independent tort of "breach of confidence." (See, e.g., Tele-Count Engineers, Inc. v. Pacific Tel. & Tel. Co. (1985) 168 Cal.App.3d 455, 462, Faris v. Enberg (1979) 97 Cal.App.3d 309, 321.) Under Faris, "[a]n actionable breach of confidence will arise when an idea, whether or not protectable [under copyright] is offered to another in confidence, and is voluntarily received by the offeree in confidence with the understanding that it is not to be disclosed to others, and is not to be used by the offeree for purposes beyond the limits of the confidence without the offeror's permission. ... There must exist evidence of the communication of the confidentiality of the submission or evidence from which a confidential relationship can be inferred. Among the factors from which such an inference can be drawn are: proof of the existence of an implied-in-fact contract [citation]; proof that the material submitted was protected by reason of sufficient novelty and elaboration [citation]; or proof of a particular relationship such as partners, joint adventurers, principal and agent or buyer and seller under the circumstances. [Citations.]" (97 Cal. App. 3d at p. 323.)

breach of fiduciary duty,[21] trade secrets[22] and

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[21] The Restatement Second of Agency generally outlines an agent's duty of loyalty. (Rest.2d Agency, §§ 387-394.) Five sections of that Restatement discuss the duty of loyalty arguably applicable here. Section 387 states: "Unless otherwise agreed, an agent is subject to a duty to his principal to act solely for the benefit of the principal in all matters connected with his agency." Section 391 states: "Unless otherwise agreed, an agent is subject to a duty to his principal not to act on behalf of an adverse party in a transaction connected with his agency without the principal's knowledge." Section 393 states: "Unless otherwise agreed, an agent is subject to a duty not to compete with the principal concerning the subject matter of the agency." Section 394 states: "Unless otherwise agreed, an agent is subject to a duty not to act or to agree to act during the period of his agency for persons whose interests conflict with those of the principal in matters which the agent is employed." Finally, section 396 extends the duty even after the agency's termination "unless otherwise agreed."

[22] Section 757 of the First Restatement of Torts outlines a cause of action for unauthorized use or disclosure of another's trade secrets. That section states: "One who discloses or uses another's trade secret, without a privilege to do so, is liable to the other if (a) he discovered the secret by improper means, or (b) his disclosure or use constitutes a breach of confidence reposed in him by the other in disclosing the secret to him, or (c) he learned the secret from a third person with notice of the facts that it was a secret and that the third person discovered it by improper means or that the third person's disclosure of it was otherwise a breach of his duty to the other, or (d) he learned the secret with notice of the facts that it was a secret and that its disclosure was made to him by mistake."

California has adopted the First Restatement of Torts' trade secret synopsis. (Uribe v. Howie (1971) 19 Cal.App.3d 194, 207-208; see generally Note, A Balanced Approach to Employer-Employee Trade Secrets Disputes in California (1980) 31 Hastings. L. J. 671; Rest.2d Torts, Introd. note to Division Nine,, pp. 1-2.) Section 757, comment b, defines a trade secret as "any formula, pattern, device or compilation of information which is used in one's business, and which gives [one] an opportunity to obtain an advantage over competitors who do not know or use it." The comment then describes the

misappropriation.[23] Paragraphs 7 through 13 of the complaint focus on the use of a wide range of confidential information that generally has nothing to do with the subject of copyright. Moreover, the claimed damages come from loss of key employees and clients.

Two other portions of the complaint, however, complicate the analysis. First, in between two of the paragraphs quoted above, Balboa pleaded: "Defendants have sold said support system and software made and owned by plaintiffs to a competitor, American Bankers Life Insurance Company and, unless restrained, will sell said support system and software, including the changes

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necessity of keeping the information secret: "a substantial element of secrecy must exist, so that, except by the use of improper means, there would be difficulty in acquiring the information. ... Some factors to be considered in determining whether given information is one's trade secret are: (1) the extent to which the information is known outside of [one's] business; (2) the extent to which it is known by employees and others involved in [one's] business; (3) the extent of the measures taken by [the proprietor] to guard the secrecy of the information; (4) the value of the information to [the proprietor] and to [the proprietor's] competitors; (5) the amount of effort or money expended by [the proprietor] in developing the information could be properly acquired or duplicated by others." (Rest. First of Torts, § 757, comm. b; see Uribe v. Howie, supra, 19 Cal.App.3d at p. 208.)

In 1984, California adopted its version of the Uniform Trade Secrets Act. (Stats. 1984, ch. 1724, § 1, codified at Civ. Code, §§ 3426-3426.10; see American Paper & Packaging Products, Inc. v. Kirgan (1986) 183 Cal.App.3d 1318, 1322-1324.) The Act, however, does not apply to misappropriations that occurred before January 1, 1985. (Civ. Code, § 3426.10.) Since plaintiffs filed their complaint in 1984, trade secret common law applies here.

[23] We have outlined the elements of misappropriation ante, page 20.

made by plaintiffs since March 4, 1981, to other competitors of plaintiffs."

Second, the complaint highlights the twin roles played in defendants' success by Maashoff's confidential information and the access to the Balboa tracking system modifications: "even with months of advance preparation, defendants' ability to induce the transfer of business from plaintiffs to Trans Global depends upon the ability of defendants to provide support service by use of the modified support system and software developed and owned by plaintiffs since March 4, 1981 and the utilization of confidential information obtained from plaintiffs by Barry Maashoff while employed as a consultant by Newport."

Unlike the broader confidential information allegations, these two paragraphs focus directly on two unauthorized uses of Balboa's software improvements. First the complaint focuses on the sale to American Bankers. In the prayer for relief, Balboa expressly requests damages for the profits derived by defendants from sale of all or any part of plaintiffs' support system and software." Second, it emphasizes the importance of Trans Global's own use of Balboa's software. By these allegations of unauthorized sale and use of software, Balboa has shifted the complaint towards areas within copyright's traditional domain.

The parties' preemption dispute thus boils down to whether the "confidential and fiduciary relationship" allegations, including trade secret, properly subsume the "unauthorized use" allegations and add the necessary "qualitatively different element" to escape preemption. For help, we turn to the copyright preemption cases involving state unfair competition claims based upon breached

confidential relationships, breached fiduciary duty, trade secrets and misappropriation.

We consider first the cases reviewing copyright preemption of trade secret law. Of the four principal cases, only one has found preemption.[24] In Videotronics, Inc. v. Bend Electronics 564 F. Supp. 1471, 1476-1477 (D. Nev. 1983), the court expressly held that copyright law preempted state law claims for misappropriation, trade secrets and unfair competition. Plaintiffs developed a computer video program called "Challenger Wild Poker." The defendants originally contracted with plaintiffs to distribute the product. Later, however, they began to manufacture and sell copies of plaintiffs' product without permission. Plaintiffs sued for violations of trade secret under Nevada law. (Id. at p. 1475.)

After reciting the Restatement's outline of trade secrets law, the court found that the defendants had not gotten the information necessary to copy the program by breaching a confidential relationship. (Id. at pp. 1475-1476.) The court found that any owner of plaintiff's game could have decoded the game's workings. Accordingly, the court found that trade secrets law itself did not protect plaintiffs. (Id. at p. 1476.)

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[24] In Avco Corp. v. Precision Air Parts, Inc. (M.D. Ala. 1980) 210 U.S.P.Q. (BNA) 894, the district court also found preemption of a purported trade secret. The court noted, however, that the complaint failed to allege invasion of privacy, trespass, breach of trust or breach of confidentiality. (Id. at pp. 897-898.)

Arguably, Avco merely held "that no trade secret claim was properly pleaded (rather than it was preempted). The court of appeals affirmed dismissal on a statute of limitation theory, and found it unnecessary to reach this issue." (Bender, supra, 47 Univ. Pitt. L. Rev. at pp. 925-926, fn. 57; see Avco (11th Cir. 1980) 676 F.2d 494.)

The court then looked to the law of misappropriation. It concluded that the copyright protection afforded plaintiffs' computer program preempted "relief under the state common law of doctrines of misappropriation and trade secret ...." (Id. at p. 1477.)[25]

Videotronics' statement about trade secret preemption is pure dicta. The court had earlier found no breach of confidential relationship under state trade secret law. Since no state trade secrets claim existed, the court should have confined itself to its misappropriation holding. Moreover, the analysis leading up to that holding lacks any discussion of how misappropriation law is equivalent to copyright. (See Bender, supra, 47 Univ. Pitt. L. Rev. at p. 927.)

Three courts have rejected claims that copyright preempts state actions based on trade secrets.[26] In

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[25] In an earlier passage, the court stated: "A property which is subject to protection under federal patent or copyright law cannot also obtain the benefit of protection under either state unfair competition or misappropriation law. . . ." (Id. at p. 1476, emphasis added.) The uncritical substitution of "trade secrets" for the earlier reference to "unfair competition" exemplifies the failure of many courts to distinguish crisply the various unfair competition theories.

[26] These cases represent the only extensive discussions. In several other cases, courts have concluded briefly or in dicta that copyright does not preempt state actions based on breached confidential relationships. (See, e.g., Foresight Resources Corp. v. Pfortmilles (D. Kansas 1989) 719 F. Supp. 1006, 1011. [Kansas Uniform Trade Secrets Act not necessarily preempted]; Vault Corporation v. Quaid Software, Ltd. (E.D. La. 1987) 655 F. Supp. 750, 763 [Louisiana Uniform Trade Secrets Act not preempted]; Boeing v. Sierracin Corp., supra, 738 P.2d 665, 674 [following Real-Time]; Freedman v. Select Information Systems, Inc. (N.D. Cal. 1983) 221 U.S.P.Q. 848, 850, 851

Warrington Associates, Inc. v. Real-Time Engineering Systems, Inc. 522 F. Supp. 367 (N.D. Ill. 1981), the plaintiff sued for wrongful appropriation and use of trade secrets from its computer programs. The court rejected the defendants' copyright preemption argument. It based its decision on a perceived lack of equivalence between copyright and trade secret.[27] The court also found passages in the legislative history of the 1976 revision to the Copyright Act that supported its view.[28] Finally, the court found that the courts of the states that provided the relevant trade secrets law "have continued to recognize causes of action for trade secret misappropriation subsequent to the amendment of the federal Copyright

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fn. 2 [preemption and trade secrets mentioned in passing]; BPI Systems, Inc. v. Leith (W.D. Texas 1981) 532 F. Supp. 208, 211 [no preemption of trade secret allegation]; see generally Bender, supra, 47 Univ. Pitt. L. Rev. at pp. 929-931.)

[27] The court stated: "It is well settled that copyright protection extends not to an idea itself, but rather to the particular expression used by its author. [Citations.] In contrast, the protection provided by the common law of trade secret misappropriation extends to the very ideas of the author, subject, of course, to the requirement that the idea has some originality and is as yet undisclosed or disclosed only on the basis of confidentiality. [Citations.] The practical distinction between the two interests is manifest. While disclosure of the expression does not vitiate rights secured by copyright law, that same disclosure may well strip the underlying idea of its confidentiality, and thus its status as a trade secret." (522 F. Supp. at p. 368.)

[28] The court cited a portion of the House Committee Report: "The evolving common law rights of 'privacy,' 'publicity,' and trade secrets, ... would remain unaffected so long as the causes of action contain elements such as an invasion of personal rights or a breach of trust or confidentiality..." (522 F. Supp. at p. 369, quoting H. Rep. No. 94-1476, 94th Cong., 2d Sess. 132 (1976) reprinted in 5 U.S. Code Cong. & Admin. News at 5746-5747 (1976).)

Act of 1976. The common law of each of these forums stresses that the trade secrets tort is based on concepts of breach of trust and confidentiality and not copying. [Citations.]." (Id. at p. 369.)[29]

In Brignoli v. Balch Hardy and Scheinman, Inc. (S.D.N.Y. 1986) 645 F.Supp. 1201, the court considered a series of state law claims arising out of a computer program's unauthorized use. Citing the "qualitatively different extra element" test, the court noted that a mere "claim that a defendant made unauthorized use of copyrightable material falls squarely within § 301 and is thus preempted. [Citation.]" (Id. at p. 1205.) Nevertheless, the court found sufficiently different "extra elements" to avoid preemption.

The court's discussion of the second and sixth causes of action is most relevant to the case before us. Concerning the second cause of action, the court stated: "Although that part of Brignoli's second claim which alleges 'willful unauthorized use of plaintiff's property' might seem to come within § 301, Brignoli's allegations that the programs are trade secrets make this claim 'qualitatively different' from a copyright claim." (Ibid.) The court then found that the sixth claim "alleges a breach of an agreement of confidentiality or duty of confidentiality. Such a claim is

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[29] The court also compared preemption analysis in patent law. It noted that the Supreme Court had found no patent law preemption of state trade secrets law. (Id. at p. 369, citing Kewanee Oil Co. v. Bicron Corp. (1974) 416 U.S. 470.) The court concluded: "If anything the congruence and, concomitantly, the likelihood of preemption, between patent and trade secret law is stronger than between trade secret and copyright law." (Id. at p. 369.) Thus, the court implied that if patent law did not preempt trade secret law, then copyright did not either.

not equivalent to a copyright claim. [Citation.]" (Ibid.) Accordingly, without more analysis, the court found that copyright preempted none of plaintiff's claims. (Id. at p. 1206.)

In M. Bryce & Associates v. Gladstone (Wis. App. 1982) 319 N.W.2d 907, the Wisconsin Court of Appeals gave the most extensive discussion of preemption matters. For three reasons, it concluded that copyright did not preempt trade secrets law.

First, it focused on the differences between copyright and trade secret law. Like the Real-Time court, it found that "[t]he line of demarcation between trade secret and copyright protection is clear. Trade secret law protects content irrespective of form of expression; copyright law protects form of expression but not the underlying ideas." (Id. at p. 915) It noted that trade secret law bars unauthorized disclosure or use of these ideas "only by persons who are privy to the trade secret by reason of some relationship to the owner which legally limits use of disclosure by them. Copyright law prohibits unauthorized copying by anyone of the form of expression in which the ideas are fixed by the author. [Citations.]" (Id. at pp. 915-916.)[30]

Second, the court also reviewed the legislative history of the 1976 and 1980 Copyright Act amendments. Although it found some confusion in the legislative history

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[30] The court may have overstated the requirement of a confidential relationship for trade secret law. (Bender, supra, 47 Univ. Pitt. L. Rev. at p. 929, fn. 76.) While such a confidential relationship usually exists, trade secret law may bar unauthorized disclosure by strangers to the secret who stumble upon it improperly or with notice of mistake. (Id; see also Restatement First of Torts, § 757.)

of the 1976 amendments, it concluded that "the thrust of the congressional discussion was in the direction of continued state protection." (Id. at p. 918.)[31] It found particular solace in a portion of the House Judiciary Committee's report on the 1980 amendments. (Ibid.) Those amendments addressed some applications of copyright law to computer software. (Ibid.) The house report stated: "The Committee consulted the Copyright Office for its opinion as to whether section 301 of the 1976 Copyright Act in any way pre-empted [unfair competition and trade secret] and other forms of state law protection for computer software. On the basis of this advice and advice of its own counsel the Committee concluded that state remedies for protection of computer software are not limited by this bill." (Ibid, quoting H.R. Rep. No.96-1307 Part I, 96th Cong. 2d Sess. (1980), pp. 23-24.)

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[31] One commentator has implicitly agreed with Real-Time and found that the 1976 amendments' legislative history weighs strongly against preemption. (See Hazen, supra, 20 U.C. Davis L.Rev. at p. 133 [citing Real-Time and Bryce].) The more exhaustive studies, however, agree with Bryce and find a confusing, even ambiguous, legislative history. (See 1 Nimmer, supra, § 1.01[B] at pp. 1-14 to 1-20.3, Scott, supra, § 3.77 at pp. 3-74 to 3-76, Bender, supra, 47 U. Pitt. L. Rev. at pp. 931-934.)

The confusion results from the deletion of an early draft bill that would have expressly not preempted state law "rights against misappropriation not equivalent to any of [the exclusive copyright] rights, breaches of contract, breaches of trust, trespass, conversion, invasion of privacy, defamation, and deception [sic] trade practices such as passing off and false representation ...." (See Bryce, 319 N.W.2d at p. 917.) The floor debate between three representatives who discussed deletion of the above text further complicates the analyses. (See Bryce, 319 N.W.2d at p. 917.) As summarized in Bryce, the three representatives "agreed that the examples should be deleted but seemed to differ on whether this action was to limit or expand preemption." (Bryce, 319 N.W.2d at p. 917.)

Third, the court reviewed the evolution of the Supreme Court's view of trade secret preemption in patent law. Two unfair competition cases from 1964 suggested an expanded federal law at the expense of state remedies. (See Sears, Roebuck & Co. v. Day-Brite Lighting, Inc. (1964) 376 U.S. 225, 232-233; Compco Corp. v. Day-Brite Lighting, Inc. (1964) 376 U.S. 234, 237-238.) In Kewanee Oil Co. v. Bircon Corp. (1974) 416 U.S. 470, 479-480, however, the court ruled that patent law does not preempt trade secret law. Bryce then concluded: "The Supreme Court in Kewanee has recognized the value of trade secrets. No significant opposition to this aspect of the Kewanee decision has been shown by Congress, particularly in view of the statutory evidence that Congress did not intend to preempt trade secret law. [¶] Since no 'unmistakable' indication has been given to the contrary by Congress and the weight of the evidence points to the recognition by Congress of the value of state protection of trade secrets, we conclude that state trade secret protection has not been preempted by the federal copyright laws." (Bryce, supra, 319 N.W.2d at p. 919.)

One factor distinguishes Bryce. Unlike Real-Time and Brignoli, Bryce arose under the 1906 copyright Act. (Id. at p. 913) That Act, however, has no express preemption clause equivalent to current section 301. (See Bender, supra, 47 Univ. Pitt. L. Rev. at p. 928, fn. 73.) Thus, its discussion of the 1976 and 1980 amendments is dicta. Nevertheless, its analysis is sound. It comports with the majority view and we adopt its reasoning.

We thus conclude that copyright does not preempt state claims based upon trade secret law. We turn to those cases involving breach of confidence. We initially note that the trade secret cases themselves suggest the

lack of preemption in the breach of confidence cases. As outlined above, trade secrets cases frequently involve confidential relationships. (See, e.g., Bryce, supra, 319 N.W.2d at p. 915; Rest.First Torts § 757.) Nevertheless, protection of trade secrets may arise even absent a confidential relationship.[32] We thus look to the cases discussing such relationships outside of the trade secret context.

"The law of confidential relationships governs duties of trust that one is not obligated to assume. Once a person commits himself to a confidential relationship, the law requires him to fulfill the duties attendant to the relationship. Confidential relation protects the trust that is implicit in relationships between employers and employees, between masters and servants, and between principals and agents, rather than the information that may pass between these parties." (Note, Federal Copyright Protection and State Trade Secret Protection: The Case for Partial Preemption, 33 Amer. Unev. L. Rev. 667, 687 (1984) [Footnotes omitted, emphasis in original].) The courts have generally found that actions for breach of a confidential relationship survive a copyright preemption challenge.

In addition to Brignoli, supra, 645 F.Supp. at pp. 1205-1206, several other courts have refused to find such claims preempted. (Walker v. Time-Life Films, supra, 784 F.2d at p. 53 [while copyright preempted general "unfair competition" claim, no such preemption of breached confidential or fiduciary relationship claims; evidence, however, insufficient to find such latter claims]; Ronald Litoff, Ltd. v. A. Kush & Assoc., Ltd. (S.D.N.Y. 1985) 621 F. Supp. 981, 986; P.I.T.S. Films v. Laconis (E.D.

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[32] See ante, footnote 29.

Mich. 1984) 588 F. Supp. 1383, 1386, Sargent v. American Greetings Corp. (N.D. Ohio 1984) 588 F. Supp. 912, 923-924; Smith v. Weinstein (S.D.N.Y.1984) 578 F. Supp. 1297, 1307; see also Litchfield v. Spielberg (9th Cir. 1984) 736 F.2d 1352, 1358 [state claim for misappropriation pre-empted but separate state claims for breach of confidential relationship dismissed without adjudication because no meritorious federal claim existed to which they could append], Mayer v. Josiah Wedgwood & Sons, Ltd. (S.D. N.Y. 1985) 601 F. Supp. 1523, 15, 36 [breach of confidential relationship possibly not preempted].)

The discussion in these cases adds little to the analysis already discussed above in the trade secrets section. We see no basis for distinguishing the cases or the theory. Accordingly, we agree that copyright does not preempt a cause of action based on breach of confidence.

We turn to the breach of fiduciary duty cases. In Del Madera Properties v. Rhodes & Gardner, Inc. (9th Cir. 1987) 820 F.2d 973, 977, the Ninth Circuit held that copyright preempted an unfair competition claim based on an alleged breach of fiduciary duty. While partners with plaintiff, the defendants had allegedly misappropriated the plaintiff's time and effort in creating certain maps and documents. The court found that the breached fiduciary duty allegation "does not add any 'extra element' which changes the nature of the action. The argument is constructed on the premise that the documents and information [one former partner] furnished to the defendants belonged to [plaintiff] and were misappropriated by the defendants. [Plaintiff's] ownership of this material, and the alleged misappropriation by the defendants, are part and parcel of the copyright claim. Thus, [plaintiff's] unfair competition claim for misappropriation of its time and

effort expended in producing the ... map and supporting documents is preempted." (Ibid.)

For several reasons, we distinguish Del Madera. First, the court cited no authority for its conclusion that copyright preempts a breach of fiduciary duty claim. In particular, the court completely ignored its earlier holding in Oddo v. Ries (9th Cir. 1984) 743 F.2d 630, 635. In that case, the court stated: "Oddo also claimed that Ries breached the fiduciary duty that Ries owed Oddo as a partner. Because a partner's duty to his co-partner is quite different from the interests preempted by copyright, this cause of action is also not preempted." (Ibid.)

Second, the Del Madera plaintiff's claim appeared to involve only the time and effort involved in creating the arguably copyrightable documents. Here, however, Balboa's alleged breach of fiduciary duty extends way beyond the unauthorized transfer of software enhancements. Given the broader allegations of breach, we do not find the claim preempted.

Several other courts have also concluded that a claim for breach of fiduciary duty survives copyright preemption. (See Walker v. Time Life Films, supra, 784 F.2d at p. 53; Ronald Litoff Ltd. v. A. Kush & Assoc. Ltd., supra, 621 F. Supp. at p. 986; Werlin v. Reader's Digest Ass'n., Inc. (S.D.N.Y. 1981) 528 F. Supp. 451, 464; see also Rand McNally & Co. v. Fleet Management Systems, Inc. (N.D. Ill. 1983) 591 F. Supp. 726, 739 [breach of fiduciary duty claim may avoid preemption]; cf. Avco Corp. v. Precision Air Parts, Inc, supra, 210 U.S.P.Q. (BNA) 894, 897-898 [trade secret claim preempted where complaint alleged no breach or trust or confidentiality].) Again, like the breach

of confidentiality cases, these cases add little analytically to the "extra element" analysis.

We see little basis for distinguishing the breached fiduciary duty claims from the breached confidential relationship and trade secret claims. They all generally involve the extra element of an important relationship. The damages flow from the disruption of that relationship, in whatever form it occurs. Here, the alleged disruption involved numerous points beyond the software claims. Accordingly, we conclude that the breach of fiduciary duty claim survives preemption.

Finally, we turn to the common law misappropriation claims. This claim's vagueness has engendered various analyses. For example, in Warner Bros. v. American Broadcasting Companies (2d Cir. 1983) 720 F.2d 231, 247, the court stated unequivocally: "state law claims that rely on the misappropriation branch of unfair competition are preempted, [citations]." Nimmer generally concludes that misappropriation that "consisted simply of the acts of reproduction and distribution ... undoubtedly constitutes a right 'within the general scope of copyright as specified by [17 U.S.C.S.] section 106.'" (1 Nimmer, supra, § 1.01[B][1] at p. 1-20.3; see also id. at pp. 1-20.5 to 1-20.6 [misappropriation by copying of musical tapes also pre-empted].)[33] At least one court, however, has found no preemption of claims. (See Sargent v. American Greetings Corp., supra, 588 F. Supp. at p. 924.)

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[33] Nimmer provides an extensive list of cases finding preemption of misappropriation type claims. (See id. at pp. 1-20.6 to 1-20.7, fn. 76.)

In the case before us, we conclude that Balboa has no common law misappropriation claim involving the software. Such a claim adds no extra element such as breach of fiduciary duty, breach of confidentiality or improper revelation of a trade secret. Absent the element of a relationship, a misappropriation claim for unauthorized use or transfer of the software adds nothing to a potential copyright infringement claim. Accordingly, copyright law preempts such a misappropriation claim.[34]

In summary, we conclude that, to the extent Balboa's complaint states claims for trade secret, breach of confidentiality and breach of fiduciary duty, it survives preemption.

II. SUBSTANTIAL EVIDENCE SUPPORTS THE JUDGMENT.

Having concluded that the trial court thus had jurisdiction to hear the unfair competition claim, we turn now to the evidence supporting the judgment. The defendant's argument boils down to four claims. First, they claim that Maashoff owed Balboa no duties of confidentiality or loyalty. Second, they claim that no trade secrets existed and that they only competed fairly. Third, they claim that Balboa's unclean hands makes equitable relief inappropriate. Finally, they challenge the trial court's damages computation. We consider each objection in turn.

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[34] Of course, to the extent the misappropriation claim does not involve Balboa's software modifications, it survives preemption. (See Del Madera, supra, 820 F.2d at pp. 976-977 [to extent defendants misappropriated effort spent producing non-copyrightable result, misappropriation claim survives preemption].)

A. MAASHOFF OWED BALBOA DUTIES OF FIDELITY AND CONFIDENTIALITY.

Defendants claim that Maashoff's status as a management consultant meant he owed Balboa no duties of fidelity or confidentiality. The court's finding's, however, demonstrate Maashoff's critical role in running Balboa's Stockton center. The court stated: "[Maashoff himself] outlined his management accomplishments, which included establishing a priority of jobs and reassignment of personnel commensurate with experience, skill and knowledge. For this management effort he was paid $1,500 a month by [Balboa]. [¶] Although he himself did not hire, fire or discipline plaintiffs' employees and did not sign checks or contacts on behalf of plaintiffs, Barry Maashoff's management suggestions were always implemented, so that through his direction and control of the office manager and supervisor he was in fact, if not in title, the effective manager in this capacity until April 26, 1984. He had access to all of the tracking system software modifications and enhancements made by [Balboa] and owed a duty of loyalty to plaintiffs."

Defendants deny only the court's conclusion. They do not contradict its basis. Indeed, Maashoff's own testimony provided much of the grounds for the court's summary. The evidence strongly suggests that his role wile a "mere management consultant" mirrored both his previous role as CPIS' tracking center manager before 1981 and his later role as Trans Global's tracking center manager. Moreover, the Stockton center's informal managerial style meant that people paid little attention to job title. Ample evidence sustains the court's express conclusion that Maashoff was in fact if not title the manager of Balboa's Stockton tracking center.

Given Maashoff's position of authority and importance in the Stockton center's operation, the trial court concluded that he owed Balboa a duty of loyalty. As noted above, an agent owes its principal duties of confidentiality and loyalty. (Rest.2d Agency § § 387-396.) In effect, defendants argue that Maashoff's independent contractor status meant that he was not Balboa's "agent" and thus owed it no duty. We disagree.

The mere label "independent contractor" does not prevent the imposition of duties of fidelity and confidentiality. An independent contractor may well be an agent. (See City of Los Angeles v. Meyers Bros. Parking System, Inc. (1975) 54 Cal.App.3d 135, 138; Rest.2d Agency § § 2(3) & 14 N.) Section 2(3) of the Restatement Second of Agency describes an independent contractor as "a person who contracts with another to do something for him but who is not controlled by the other nor subject to the other's right to control with respect to his physical conduct in the performance of the undertaking. He may or may not be an agent." Section 14 N further states: "One who contracts to act on behalf of another and subject to the other's control except with respect to his physical conduct is an agent and also an independent contractor." In contrast, comment b to section 14 N describes a "non-agent independent contractor": as "[a] person who contracts to accomplish something for another or to deliver something to another, but who is not acting as a fiduciary for the other .... He may be anyone who has made a contract and who is not an agent. The term is used colloquially to describe builders and others who have contracted to accomplish physical results not under the supervision of the one who has employed them to produce the results." (Rest.2d Agency § 14 N, comm. b.)

The determination of agency status from conflicting evidence normally presents a question for the trier of fact. (2 Witkin, Summary of Cal. Law (9th ed. 1987), Agency and Employment, § 37, at p. 50.) On undisputed evidence, however, determination of agency presents a question of law. (See 9 Witkin, Calif. Procedure, supra, Appeal, § § 242 & 290.) Here, the evidence of Maashoff's role is largely unconflicting. The inferences from that evidence, however, conflict sharply.

Generally, a principle authorizes an agent to use discretion in carrying out the principal's purposes in transactions with third persons. (See, e.g., Workman v. City of San Diego (1968) 267 Cal.App.2d 36, 38.) "The existence of [a] right of control and supervision [in the principle] establishes the existence of an agency relationship. [Citation.]" (Malloy v. Fong (1951) 37 Cal.2d 356, 370.)[35] By imposing a duty of loyalty upon Maashoff, the trial court implicitly found him Balboa's agent and subject to its control. Based on our review of the record, we agree with this implicit conclusion.

Balboa hired Maashoff to shape up the Stockton center's operations. He became the de facto head of a

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[35] Malloy noted that "[o]ther tests are sometimes invoked, in addition to the power of control, in determining whether one is an agent." (Ibid.) The court then listed eight considerations: (a) is the performer of services engaged in a distinct occupation or business; (b) in the locality, do unsupervised specialists or supervised workers usually perform such services; (c) what kind of skills does the service require; (d) who supplies the tools and workplace; (e) how long does the employer require the services; (f) does the employer pay by time or by job; (g) does the employer usually do this kind of work; and (h) what kind of relationship do the parties believe they created? (Id. at pp. 371-372.)

management troika that included department supervisors Jan Mehlhaff and Darryl Fenley. Maashoff would make "suggestions" to Mehlhaff and Fenley. His suggestions were always adopted. Balboa's headquarters people considered Maashoff the party ultimately responsible at the Stockton office. Maashoff's decisions involved the specific duties of many of Balboa's Stockton center employees.

At the same time, Balboa retained control over Maashoff's acts. For example, Balboa strictly limited Maashoff's powers. He had no authority to talk to Balboa's agents directly and no power over hiring, firing, and disciplining the other employees. Maashoff reported to Balboa through its headquarters employee, Sharon Paolino. Part of her duties involved communicating Balboa's decisions back to Maashoff. Taken together, the record shows sufficient evidence of Balboa's retained power over Maashoff.

As Balboa's agent, Maashoff thus owed it duties of fidelity and confidentiality.

B. MAASHOFF BREACHED HIS DUTIES TO BALBOA.

Defendants claim that even if they owed duties to Balboa, no breach occurred because they competed fairly. In particular, they claim that none of the information they supposedly appropriated was confidential or a trade secret. In addition, they claim that they had a right to open a competing center, hire Balboa's former employees and lure Balboa's former clients. The circumstances belie their argument.

We consider first the trade secret claim. Defendants argue that the record contains no evidence that any of the supposedly appropriated information was a trade secret. Prior to trial, however, the parties stipulated that their computer programs were trade secrets. They brought this stipulation to the trial court's attention. Dold's testimony alone demonstrated numerous portions of Balboa's system modifications ended up in Trans Global's software.[36] Maashoff had access to all of the modifications through his direction of the computer programmers. Maashoff, through his presidency of CPIS, was instrumental in the transfer of these modifications to American Bankers and Trans Global.

Moreover, the evidence also showed that Maashoff had one of Balboa's programmers bring to him at Trans Global three or four new Balboa programs for completion. By all accounts, she had completed substantial portions of those programs before she spent her vacation finishing them at Trans Global's new center with Maashoff. The record thus amply demonstrates Maashoff's direct assistance in the wrongful appropriation of the trade secret.

The parties argue whether Balboa's client list or employee identities meet the test for trade secrets. Under some circumstances, courts have held that trade secret

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[36] Defendants argue that the number of lines copied was trivial. They also claim that any copying was inadvertent.

A brief comparison of some of the programs suggests more than a trivial identity between Balboa's modifications and Trans Global's program. Moreover, Dold testified that the bare number of program lines alone did not necessarily reveal a given modification's significance. In addition, he testified that the manner of duplication did not suggest inadvertence.

law protects against unauthorized use of client lists. (See, e.g., Klamath-Orleans Lumber, Inc. v. Miller (1978) 897 Cal.App.3d 458, 464-466 [appropriation of confidential customer list by former employees gave that employee an unfair ability to solicit customers more selectively and more effectively.]; see generally, Note, A Balanced Approach to Employer-Employee Trade Secrets Disputes in California (1980) 31 Hastings L.J. 671, 675-687 ["The type of trade secret most frequently the subject of litigation between a former employer and employee in California is the customer list."]; The Law of Competitive Business Practices (Cont.Ed.Bar. 1981) pp.125-134.) Courts have also prevented unfair raiding of employees. (See, e.g., Bancroft-Whitney Co. v. Glen (1966) 64 Cal.2d 327, 352-353.) Each unfair competition case, however, turns on its own unique facts. (Id. at pp. 346-347.) As one court stated, "the determination of whether a particular business practice is unfair necessarily involves an examination of its impact on its alleged victim, balanced against the reasons, justifications and motives of the alleged wrongdoer. In brief, the court must weigh the utility of the defendant's conduct against the gravity of the harm to the alleged victim--a weighing process quite similar to the one enjoined on us by the law of nuisance." (Motors, Inc. v. Times Mirror Corp. (1980) 102 Cal.App. 3d 739, 740 [discussing "unfair competition" under Bus. & Prof. Code § 17200].)

We need not determine, however, whether the lists and identities here technically were trade secrets. In this case, the sum of the actions speak louder than any of the individual parts. Rather, we shall conclude that Maashoff breached his duty of fidelity and confidentiality to Balboa by setting up a competing business and luring Balboa's clients and employees away unfairly.

Substantial evidence shows that the success of Trans Global's new venture depended upon the ability of the defendants to offer Balboa's clients a complete service package that duplicated as much as possible the procedures and personnel from Balboa's Stockton center. Two of the clients described the defendants' sales pitch. One client, a banker, said that one of the CFIA agents told her that if her bank switched, "there will be no changes in the tracking, that [the bank] would be dealing with the same people basically that had been handling the accounts for [the bank]." The agent also told her that Trans Global had access to enough information so that the bank would not have to go through an audit if it switched. In sum, the agent said that "the only change in the procedures that [the bank] would be going through would be the fact that the 800 toll free number ... would be a different number now." The agent kept emphasizing that "the procedures would remain the same, that [the bank] would not have to learn any new ones."

The other client, an insurance agent who wrote for Balboa, described virtually an identical sales pitch. Discussing the importance of continuity, that client noted "any kind of change is always a trauma for anyone." His comments echoed the unequivocal testimony of a Balboa employee who had worked in the Stockton Center: "The lenders were always fearful of a conversion because it always disrupted their customer base." A system changeover entailed a lot of work: "[e]very loan virtually is touched, and when you're dealing with that quantity, there are bound to be errors, and the errors are magnified because everything is touched."

In this light, Maashoff's position became critical to defendants' ability to compete at all. Viewed in the light

most favorable to upholding the judgment, the record reveals a pattern of conduct in derogation of his duties of confidentiality and loyalty to Balboa. While still managing Balboa's center, Maashoff reviewed a list of the strengths and weaknesses of Balboa's department supervisor shortly after preparing a list of Trans Global's staffing needs. He then solicited at least three of Balboa's employees directly, and attempted to create a "loyal base" among the other Balboa employees. Moreover, he kept all of this information secret from Balboa until he could present it with a fait accompli.

Again, while still Balboa's manager, Maashoff helped plan the solicitation of Balboa's clients. These included clients that CPIS' debt and Maashoff's debt guarantee. He also told the clients of lender account tapes that Balboa kept and urged the clients to demand the information from Balboa. At the same time, he left instructions for Balboa's employees to delay notifying Balboa of some of the requests. Finally, shortly after leaving Balboa, he urged a Balboa employee to organize an employee walkout.

In conjunction with the computer software transfer to Trans Global outlined above, the record shows a pattern of conduct that goes beyond legitimate competition between an agent and its former principal. Even if each individual component of Maashoff's master plan did not breach his duties to Balboa, the whole certainly did. (Bancroft-Whitney, supra, 64 Cal.2d 327, 348.)

In Bancroft-Whitney, the supreme court reviewed the conduct of Bancroft-Whitney's (BW) former president and director, Judson Glen. While still BW's officer and director, Glen began plans to assist BW rival Matthew

Bender to set up a new regional office. After he reviewed the strengths and weaknesses of key BW employees, Glen solicited a number away. He did it in part by telling BW to delay a salary increase and then getting Bender to offer more money immediately. (Id. at p. 348.)

The court summarized the applicable law. "There are only a few cases ... which involve the specific question whether an officer may offer employees of his corporation jobs with a competing enterprise he is preparing to join. The cases are not consistent in their results and appear to rest on general principles relating to the obligations of the fiduciary. [Citations.] The mere fact that the officer makes preparations to compete before he resigns his office is not sufficient to constitute a breach of duty. It is the nature of his preparations which is significant." (Id. at pp. 345-346.)[37]

The court then discussed the duty to reveal the plans to compete. "There is no requirement that an officer disclose his preparations to compete with the corporation

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[37] At this point, the court cited comment to section 393 of the Restatement Second of Agency. As set forth above, that section deals with a former employee's use of confidential information in competition with the former employer. The court included illustration 1. (Id. at p. 346, fn. 10.) that illustration states: "A is employed by P as manager for a year. Before the end of the year, A decides to go into business for himself; in anticipation of this and without P's knowledge, he contracts with the best of P's employees to work for him at the end of the year. At the end of the year, A engages in competing business and employs the persons with whom he has previously contracted. A has committed a breach of his duty of loyalty to P." (Emphasis added.)

Maashoff's conduct here mirrors almost identically the conduct proscribed by illustration 1.

in every case, and failure to disclose such acts will render the officer liable for a breach of his fiduciary duties only where particular circumstances render nondisclosure harmful to the corporation. [Citations.] Conversely, the mere act of disclosing his activities cannot immunize the officer from liability where his conduct in other respects amounts to a breach of duty. The significant inquiry in each situation is whether the officer's acts or omissions constitute a breach of trust under the general principles applicable to the performance of his trust." (Id. at p. 347.)

Turning to the case before it, the supreme court found undisputed evidence of "a consistent course of conduct ... designed to obtain for a competitor those of [BW's] employees whom the competitor could afford to employ and would find useful. ... We need not decide whether any of these acts would constitute a breach of fiduciary duty, taken alone, since there can be little doubt that, in combination, they show a course of conduct which falls demonstrably short of 'the most scrupulous observance' of an officer's duty to his corporation." (Id. at pp. 347-348.) The court then found that Bender's complicity in Glen's breach of fiduciary duty amounted to unfair competition. (Id. at p. 353.)

Defendants try to distinguish Bancroft-Whitney because the defendant there was a corporate officer while Maashoff was a management consultant. The attempt fails. As set forth above, Maashoff's status as Balboa's agent imposes duties of fidelity and confidentiality. Here, in addition to such conduct, Maashoff helped accomplish the entire plan of establishing the competing center. On the facts of this case, Maashoff breached his duties of fidelity and confidentiality. By encouraging, ratifying and accepting the benefits of Maashoff's breach, the other

defendants competed unfairly. (Bancroft-Whitney, supra, 64 Cal.2d at pp. 353-355.)

C. THE COURT PROPERLY REJECTED THE UNCLEAN HANDS DEFENSE.

Defendants next claim that Balboa's unclean hands make its claim for damages inequitable. In the court below, defendants originally labelled their defense: "breach of the covenant of good faith and fair dealing."[38] They then argued "unclean hands" in their new trial motion. By rejecting that motion, the trial court implicitly rejected the unclean hands defense. We see no error in the ruling.

Essentially, defendants claim that Balboa attempted to sell to CFIA's insurance clients directly in order to cut out the agents' commissions. In addition, they claim that Balboa failed to put new business on the Stockton tracking system.

The evidence of both claims conflicted sharply. Maashoff, however, himself testified that Balboa had paid him all commissions due. No other evidence suggested that any other CFIA agent lost commissions due them. Moreover, the record contains none of the contracts between Balboa and the various insurance agents. Absent some evidence of what those agreements contained in light of trade practices, we cannot say that Balboa's decision to

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[38] The statement of decision does not directly discuss this defense. nevertheless, defendants do not predicate their claim of error on the statement of decision's failure to address this defense. Under the circumstances, it appears that defendants converted this defense to "unclean hands."

cancel agents' contracts amounted even to a breach of contract, much less unclean hands.

Whatever the gravity of Balboa's decision to place new business on its Irvine system, it does not approach the egregiousness of defendants' conduct. Indeed, we have difficulty conceiving that defendants had any substantial basis for seeking affirmative relief against Balboa. In any event, defendants' complaints against Balboa did not give them a license to seek retribution by breaching duties of fidelity and confidentiality. (See Fibreboard Paper Products Corp. v. East Bay Union of Machinists (1964) 227 Cal.App.2d 675, 729.) We find no error in the court's rejection of the unclean hands defense.

D. BALBOA PROVED ENTITLEMENT TO THE DAMAGES AWARDED.

Defendants raise three objections to the amount of damages the court awarded for the lost insurance business. First, they claim that Balboa could have mitigated its losses by agreeing to let Trans Global track the loans for a fee. Second, they claim that they disproved a key element of the formula Balboa used to calculate its loss. Finally, they claim that the court should have discounted the award to its present cash value. None of their objections has merit.

We look first to Balboa's duty to mitigate its losses by doing business with Trans Global. As defendants themselves note, Balboa need only take reasonable steps to mitigate losses. (See, e.g., 6 Witkin, Summary of Cal. Law (9th ed. 1988) Torts, § 1382, at p. 852.) By refusing to reduce the damages award, the trial court implicitly found that it would be unreasonable to have forced Balboa to do

business with Trans Global. We see no basis for disturbing this ruling.

As the trial court noted, Maashoff's "plan" presented Balboa with a fait accompli: either do business with Trans Global for a fee or lose all your accounts. By this time, Balboa could well have desired to wash its hands entirely of Maashoff and company. The "plan" attempted to coerce a tracking service commission where none would otherwise be due. More importantly, it arose against the entire background of the parties' relationships. By casting its lot with Maashoff and company, Balboa had already experienced CPIS' repeated failure to pay off on its debt; CPIS' "out of trust" situation where it had diverted hundreds of thousands of dollars of premiums owed Balboa; and the transfer of its software modifications to American Bankers. Under all these circumstances, Balboa had no duty to accept the "invitation" to do business with the former agent who had just breached duties of fidelity and confidentiality by setting up a competing tracking center.

We turn next to the court's decision to adopt Balboa's formula for computing its lost profit. Balboa's employee, Alex Majzuob, testified that Balboa annually retained 94.4 percent of the accounts on its system at the start of each year. Majzoub then determined the total profits Balboa had earned in the previous year from the accounts Trans Global took from Balboa. He multiplied the profitability figure by the 94.4 percent retention rate 25 times and determined lost profits over a twenty five year period. This totaled $3,721,000.

Defendants claim that their testimony refuted Majzoub's 94.4 percent retention rate. They claim that they showed that Balboa had experienced a much lower

retention rate on the particular accounts that it had ever tracked at its Stockton center. Accordingly, they argue that the court should have used a retention rate based solely on the accounts Balboa had handled at Stockton. We disagree.

Even assuming that defendants have proffered undisputable evidence of a lower retention rate on Balboa's Stockton accounts, the trial court did not err by adopting Majzoub's figure. Majzoub's figure represented a broader sample of Balboa's experience with the collateral insurance tracking services and products. It included other Balboa serviced from its Irvine system. The inclusion of the other data gave Balboa's retention rate calculations "a larger piece of data for reliability."

Defendants show us no reason why Balboa should not have included its broader sample in calculating its retention rate. Given all the bugs in the Stockton center that Balboa had paid to straighten out, its retention rate on those accounts might well have been abnormally low. No error comes from the court's decision to use the 94.4 percent figure.[39]

Defendants next claim that the court erred by refusing to reduce the lost profit award to its present cash value. At trial, however, they introduced no evidence from which the court could choose an appropriate discount rate

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[39] Similarly, we do not find any error in using the 25 year time period. While Majzoub admitted that he could have used other periods to calculate the lost profits, under his formula, Balboa still showed lost profits through the year 25. By limiting itself to a 25 year period, Balboa elected to waive and claim for damages it might otherwise have demonstrated.

nor did they request that the court take judicial notice of "present cash value" tables. (Compare Wilson v. Gilbert (1972) 25 Cal.App.3d 607, 613 [absent evidence of discount rates, court properly refused jury instruction on present cash value].)

Moreover, the court expressly noted that its non-discounted award adequately offset likely increases in Balboa's future returns. Balboa had introduced evidence that both inflation and its growing volume of business would likely increase future premiums and profits. Nevertheless, Majzoub's formula did not include such probable increases in profits from the accounts Trans Global took. Accordingly, the court concluded: "[c]onsidering all of these circumstances, ... $3,721,000 ..., which projects no growth within any of the accounts on the Stockton system, is as fair an approximation of present value of the loss suffered by plaintiffs as can be determined at this time, in effect offsetting future growth against discounts to present value, both of which attempt to anticipate future events and are similarly speculative."

In light of defendants' complete failure to introduce any evidence so that the court could compare projections of the relative rates of inflation, future business growth, and the cost of money, the court did not err by calling the matter a wash. We see no error in the court's calculation of damages.

E. THE JUDGMENT CORRECTLY INCLUDES CFIA AND CFIA OF NEVADA.

Defendants next claim that no evidence supports the judgment against CFIA and CFIA of Nevada. As set forth above, CFIA ran the insurance agents in Stockton who

sold the Balboa insurance to the banks and credit unions. CFIA of Nevada performed a similar function for a number of Nevada based accounts.

The record contains substantial evidence from which the court could have found that CFIA and CFIA of Nevada ratified and accepted the benefits of the improper acts of Maashoff, CPIS and Trans Global. For example, Jack Nelson was intimately involved with both companies as well as CPIS. On April 30, 1984, Nelson wrote one of the Nevada customers to explain the changes in tracking services and underwriters. In that letter, he explained that CFIA had "formed a Joint Venture with another firm, [Trans Global]. The Venture, [Trans Global Financial Services], is being managed by our firm. This Joint Venture, which utilizes our loan tracking system software on the latest "state-of-the-art" Hewlett Packard computer hardware, commenced operations as of April 1, 1984. [¶] The staff for our new service center is the same experienced staff that has been providing service to our lender clients for many years, in that they changed their employment status from [Balboa] to the Joint Venture." (Emphasis added.)

This letter alone shows CFIA of Nevada's complete acceptance of the benefits of the unfairly competitive acts. Given the overlap of officers, directors, and shareholders between CPIS, CFIA and CFIA of Nevada, it strains credulity to believe that CFIA of Nevada accepted those benefits ignorant of the circumstances.

CFIA's liability appears even more evident. Maashoff was its president, a director and a shareholder. He testified that he wanted to break from Balboa in order to protect the commissions earned by the insurance agents

CFIA ran. The court did not err by holding CFIA accountable for its president's avowed efforts to save its business.

III. AMPLE AUTHORITY SUPPORTS THE TRIAL COURT'S APPOINTMENT OF DOLD AS AN EXPERT WITNESS.

Defendants claim that the trial court lacked authority to appoint Dold as an expert witness. We disagree. Evidence Code section 730 states: "When it appears to the court, at any time before or during the trial, that expert evidence is or may be required by the court or by any party to the action, the court on its own motion or on motion of any party may appoint one or more experts to investigate, to render a report as may be ordered by the court, and to testify as an expert at the trial of the action relative to the fact or matter as to which such expert evidence is or may be required." This section thus provides ample authority for Dold's appointment.

Without citation to any statute or case, defendants claim that section 730 "is invoked primarily in criminal and juvenile proceedings where necessary to assist the court." No such limitations appear on the statute's face. Evidence Code section 300 makes section 730 generally apply "in every action before the ... superior court." Section 105 defines action to include "a civil action and a criminal action." We know of no reason to except section 730 from applicability to a complicated case involving computer software. Accordingly, we find no error in Dold's appointment.

IV. MAASHOFF IS PERSONALLY LIABLE FOR HIS BREACHES OF DUTY.

Despite the court's express findings that "Barry Maashoff breached his duty of loyalty to plaintiffs ...," the court refused to hold him accountable personally. Rather, it concluded, "that there is insufficient evidence to impose personal liability upon the individual defendants ... [including] Barry Maashoff." Balboa has cross-appealed from this part of the judgment.

We agree with Balboa that the court's ruling on Maashoff's individual liability conflicts with the court's underlying judgment against the business entity defendants. As set forth above, the trial court predicated substantial portions of the judgment upon Maashoff's conduct. As outlined above, as its agent Maashoff owed a duty personally to Balboa. As principal, Balboa has a right to proceed against Maashoff individually. "An agent is subject to liability for loss caused to the principal by any breach of duty." (Rest.2d Agency § 401; see generally id. at § § 399-406 [remedies available to principal against agent.].)

Maashoff's duty is personal and results from his relationship to the plaintiffs, not his relationship as an officer, director, investor or employee of defendants. While the latter relationships support the court's findings that the entity defendants ratified Maashoff's conduct as their own, that ratification does not shield Maashoff from his direct liability to Balboa. (See generally 5 Witkin, Summary of Calif. Law (9th ed. 1988) Torts, § 34, at p. 94 [corporate officers liable for torts committed by them on corporation's behalf if they participate in, authorize or direct the wrong].)

V. DISPOSITION

We reverse that portion of the trial court's judgment in favor of Barry Maashoff individually. We order judgment entered in favor of Balboa against Barry Maashoff individually for $3,721,000.[40] In all other respects, we affirm the court's judgment. Defendants and cross-respondent are ordered to assume Balboa's costs on appeal equally.

s/ Davis, J.

We concur:

s/ Evans, Acting P.J.

s/ Marler, J.

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[40] Balboa does not argue that Maashoff should also share liability for the portion of the judgment involving the tracking system license sales to American Bankers and Trans Global. Accordingly, we limit direction of judgment to the damages for loss of the insurance accounts.

COURT OF APPEAL OF THE STATE OF CALIFORNIA

THIRD APPELLATE DISTRICT

BALBOA INSURANCE CO., et al.,

Plaintiffs, Respondents and Cross-Appellants,

v.

TRANS GLOBAL EQUITIES, et al.,

Defendants, Appellants and Cross-Respondent

3 Civil C000793

FILED April 19, 1990

By the Court:

Appellants' petition for rehearing is denied.

Dated: April 19, 1990

EVANS, Acting P.J.

ORDER DENYING REVIEW

AFTER JUDGMENT BY THE COURT OF APPEAL

Third Appellate District No. C000793

S015325

IN THE SUPREME COURT

OF THE

STATE OF CALIFORNIA

IN BANK

BALBOA INSURANCE COMPANY, Et Al.,

Appellants,

v.

TRANS GLOBAL EQUITIES, Et Al.,

Respondents.

Appellants' petition for review DENIED.

/s/ Lucas
Chief Justice

Filed June 7, 1990

SUPERIOR COURT OF CALIFORNIA

COUNTY OF SAN JOAQUIN

BALBOA INSURANCE COMPANY, et al.,

Plaintiffs,

v.

TRANS GLOBAL EQUITIES, et al.,

Defendants.

No. 176696

STATEMENT OF DECISION

FILED JULY 18, 1986

The above entitled case was heard by the court sitting without a jury.

Darrell Glahn, Esq. and Donald West, Esq. appeared for plaintiffs.

George R. Corey, Esq. of Corey, Orton, Luzaich & Gemello and Velma Lim, Esq. of Kroloff, Belcher, Smart, Perry & Christopherson appeared for defendants.

The evidence discloses that some years before 1979, John Nelson began a loan collateral tracking service which

eventually became known as Collateral Protection Insurance Services (CPIS). In October, 1979, to finance continued work on the computerization of that tracking system, CPIS borrowed $500,000.00 from Balboa Insurance company and undertook to write collateral loan coverage with the Balboa Insurance Group (Balboa). In the spring of 1980 CPIS and its principals were unable to pay to Balboa the premiums for insurance written. They had diverted the money collected as premium payments to other uses and were "out of trust". They likewise were unable to make the payments due toward retirement of the $500,000.00 borrowed. As a result of the foregoing, in June, 1980, CPIS and its principals executed a note in favor of Balboa to cover the out of trust sum, and gave as security the computer software being developed for the tracking system. Before March 1, 1981 CPIS and Martin Atherton had developed the basic or core programs of a computerized on-line insurance follow-up system for the tracking of loan collateral, hereinafter referred to as the tracking system software.

In January, 1981 John Nelson advised Balboa that CPIS and its principals were unable to make payment on the obligations to Balboa. As a result, a series of contracts was entered into on March 1 and March 4, 1981 (Exhibits 1(a) through (d)) consisting of four agreements involving six entities.

Exhibit 1(a) is a perpetual non-exclusive license of the software from Collateral Protection Insurance Services (CPIS) to Newport Management Company (NMC), a member of the Balboa Insurance Group. By the terms of that license agreement, NMC had the right to modify said tracking system software and all modifications and enhancements made by NMC became the property of

NMC. On March 4, 1981 CPIS was the owner of said tracking system software, subject to a security interest held by Martin Atherton. Martin Atherton consented to this license in writing on the license agreement.

Exhibit 1(b) is a special override commission agreement between CPIS and NMC, which is the consideration for the license.

Exhibit 1(c) is an agreement between John F. Nelson and Balboa Insurance Company under which Nelson agreed to refrain from taking any action to cause termination of the Exhibit A accounts sold by Exhibit 1(d), as well as certain other account master policies, designated Exhibit B, in return for his release from certain obligations of CPIS he had personally guaranteed in 1980 and Balboa's agreement to restructure certain CPIS obligations. This personal undertaking by Nelson was limited to six months.

Exhibit 1(d) is the contract of sale of certain accounts, denominated the "Exhibit A" accounts, from CPIS and Consolidated Financial Insurance Agency (CFIA) to Balboa Insurance Company, in which the sellers agreed to do nothing to cause the policies comprising that business to be cancelled, lapse or otherwise terminate.

Prior to March 1, 1981, Barry Maashoff was manager of the loan collateral tracking center operated by defendants. On March 1, 1981, NMC began operating that facility as plaintiffs' Stockton Service Center, paying all expenses, including rent, payroll, equipment lease, utilities, etc. Barry Maashoff managed the Stockton Service Center for NMC for six months. He then devoted his efforts to development of sales for CPIS and Balboa

nationwide for the next fifteen months. In December, 1982 he returned in a management capacity for NMC as "management consultant" for the Stockton operation. By his own testimony Barry Maashoff admitted that in December, 1982 he again assumed responsibility with respect to the Stockton service center and described himself as a "management consultant" for plaintiffs. His job was to assist the Stockton service center to function in an efficient manner, to achieve which he made recommendations and directed certain things to be done to get the work out in an efficient manner; he made any changes which might appear necessary to improve efficiency "within some limitations". His suggestions included job assignment of service center personnel in order to get the right job done at the right time, which he described as the "ultimate management objective."

Barry Maashoff's management style was indirect, he worked through Sharon Paolino initially and then through Darryl Fenley and Jan Mehlhaff, the first line supervisors. He followed the same management pattern when he returned in December, 1982 as he had used in 1981. In Exhibit 5 he outlined his management accomplishments, which included establishing a priority of jobs and reassignment of personnel commensurate with experience, skill and knowledge. For this management effort he was paid $1,500 a month by NMC.

Although he did not himself hire, fire or discipline plaintiffs' employees and did not sign checks or contracts on behalf of plaintiffs', Barry Maashoff's management suggestions were always implemented, so that through his direction and control of the office manager and supervisors he was in fact, if not in title, the effective manager and remained in this capacity until April 26, 1984. He

had access to all of the tracking system software modifications and enhancements made by NMC for plaintiffs and owed a duty of loyalty to plaintiffs.

The net effect, in addition to relieving the CPIS defendants of the $702,000 obligation, was to relieve them of the service center overhead and the continuing software development cost and to continue in operation the tracking system service center which was processing the business of defendants CPIS, CFIA, Maashoff and Nelson, thus enabling them to carry on their business.

Beginning in March, 1981, NMC employed Martin Atherton and others to continue development of the tracking system software, correcting logic and progamming errors and making extensive modifications and additions to the basic programs, all of which significantly improved the operation of the system both for the operator and the user. These modifications and enhancements are the property of NMC; CPIS has no right to sell or otherwise use them.

In early 1983, CPIS sold a license of the tracking system software to American Bankers Insurance Company. The system delivered by defendants to American Bankers Insurance Company was the then current system, which included the software modifications owned by NMC. In the summer or fall of 1983, CPIS and its principals began discussing with the principals of Trans Global the establishment of a service center to compete with Balboa's Stockton Service Center. In January, 1984, CPIS and Trans Global entered into a joint venture agreement for the establishment of such competing service center. The center was operational by April, 1984.

Defendants obtained from Barry Maashoff and Martin Atherton and used the then current NMC tracking system software in establishing their competing service center's tracking system, including the modifications and enhancements made and owned by NMC. Defendants were not authorized by plaintiffs to use or sell plaintiffs' modifications and enhancements or to sell or use the tracking system software with plaintiffs' modifications and enhancements contained in it. Nevertheless, defendants exercised dominion and control over plaintiffs' tracking system software inconsistent with plaintiffs' ownership of said software by using it in the tracking system of the Trans Global service center. Defendants Barry Maashoff, Jack Nelson and CPIS also exercised dominion and control over plaintiffs' tracking system software by selling the same to American Bankers Insurance Company.

The content and working of the tracking system software modifications and enhancements made by plaintiffs were not generally known except to persons employed by plaintiffs; defendants knew of them because defendants caused Martin Atherton and Barry Maashoff to provide such information to them.

In the spring of 1984 defendants caused Barry Maashoff to solicit and hire away from plaintiffs certain key employees of plaintiffs' Stockton Service Center while he was employed by plaintiffs there.

While employed by plaintiffs, Barry Maashoff breached his duty of loyalty to plaintiffs by managing the establishment of a competing service center for defendants, by hiring away for defendants certain of plaintiffs' key Stockton Service employees, by providing to defendants plaintiffs' modifications and enhancements to the

tracking system software and by selling plaintiffs' tracking system software modifications and enhancements to American Bankers Insurance Company. By the time April 4, 1984 conversation with Jack Trapp to which Barry Maashoff testified, defendants had completed their preparations for opening a competing tracking center. The April 4 discussion was not a warning of future events, but a statement of an accomplished fact.

Barry Maashoff was at all times on and after March 1, 1981, an officer and director of Collateral Protection Insurance Services and in the spring of 1984, was an officer and director of Trans Global Financial Service Center, Inc. and, as such, his acts were the acts of said defendants. Collateral Protection Insurance Services, Consolidated Financial Insurance Agency, Consolidated Financial Insurance Agency of Nevada and the Trans Global enterprise in its various forms accepted the benefits of and ratified the actions of Barry Maashoff herein specified.

Unfair Competition

The complaint states only one cause of action, for unfair competition. Plaintiffs' counsel's insistence there are four causes of action at issue, with four theories of recovery, is incorrect.

Substantial evidence in the record demonstrates a breach of the contractual provision of plaintiffs' Exhibit 1(d) that defendants would take no action to cause the assigned policies of insurance to be cancelled, lapse or otherwise terminate. However such breach of contract is pertinent only insofar as it may constitute unfair competition.

Substantial evidence in the record demonstrates that the defendants have converted to their own use (or sold to others) the software modifications that belong to plaintiffs. Such conversion is likewise pertinent only insofar as it may constitute unfair competition.

Although the evidence shows defendants conspired, the complaint contains no cause of action for conspiracy nor any allegations that the defendants conspired to compete unfairly against plaintiffs.

A constructive trust could be an appropriate remedy here, but there is no cause of action for imposition of a constructive trust on the proceeds of sale of the CPI support system containing plaintiffs' modifications, nor does the prayer contain a request for the imposition of a constructive trust.

Plaintiffs contend they have established a case of unfair competition by the defendants in the following instances:

1. The defendants solicited away the insurance accounts that had been assigned to Balboa in satisfaction of the $702,000 indebtness of CPIS;

2. The setting up of a competing tracking center and siphoning away of plaintiffs' business at their Stockton service center by use of confidential information obtained by defendant Barry Maashoff while employed in a management capacity at plaintiffs' Stockton service center, including at least, software programming, information relating to specific current needs and desires of particular accounts and knowledge of the working and idiosyncracies of the account personnel as well as employee information and evaluation.

3. The hiring away of plaintiffs' key employees at the Stockton service center; and

4. The sale and unauthorized use of plaintiffs' software modification built into the CPIS support system.

Plaintiffs rely heavily upon Bancroft-Whitney v. Glen, 64 C.2d 327, where Glen, the former president and director of Bancroft-Whitney, while still acting in that capacity, signed a contract with a law book publisher competitor, Matthew Bender and Co., to set up a western division of that firm, and in so doing, violated his duties owing to Bancroft-Whitney.

Barry Maashoff is not in exactly the same position as Glen, since Maashoff was never an officer of any of plaintiff corporations and at all times was director and officer of defendant CPI. The fact that Maashoff was employed by Balboa in a management capacity at the Stockton service center is significant only in that it enabled him to obtain access to confidential information which he was able to use to plaintiffs' detriment and defendants' benefit.

More applicable to plaintiffs' claim of trade secret piracy is the unfair competition case of A & M Records, Inc. v. Heilman (1977) 75 C.A.3d 554. In that case, defendants advertised and sold record and tape albums which included performances of songs duplicated from recordings manufactured by plaintiff, without paying plaintiff for same. This was a clear case of record and audio-tape piracy. It was held unfair competition.

The court finds that the plaintiffs have sustained their burden of proof as to the allegations of unfair competition in the following instances:

1. The defendants solicited and took Exhibit "A" accounts sold to plaintiffs in 1981.

By the terms of the 1981 contract, the CPIS defendants sold the Exhibit "A" accounts to plaintiffs and expressly covenanted that they would do nothing to cause said accounts to terminate their relationship with plaintiffs. Defendants have, however, caused many of said accounts to leave plaintiffs for defendants.

2. Defendants, together with Barry Maashoff and utilizing his efforts in his management capacity for plaintiffs, hired away certain key employees from plaintiffs' Stockton Service Center.

Barry Maashoff evaluated the employees of plaintiffs working at the Stockton Service Center and discussed their qualifications with their immediate supervisor to determine which of the employees defendants should solicit to work at the Trans Global tracking center. He then did solicit those employees of plaintiffs he desired and succeeded in hiring certain of them.

3. Defendants utilized the managerial efforts of Barry Maashoff to create a competing loan tracking service for Trans Global.

In the winter and spring of 1984 Barry Maashoff laid out the facilities, ordered computer equipment, arranged for telephone service, hired employees and otherwise made sure the competing Trans Global tracking service facility was prepared for operation by April, 1984.

4. Defendants obtained from Barry Maashoff and Martin Atherton plaintiffs' tracking system software and utilized it in setting up the Trans Global tracking system.

Defendants hired Martin Atherton to write the Trans Global tracking system software. He used a tape containing many of plaintiffs' modifications as the basis of the Trans Global tracking system. Barry Maashoff obtained tapes of plaintiffs' current programming from other of plaintiffs' employees and furnished the same to defendants. Plaintiffs' modifications from these sources were incorporated in the Trans Global tracking system software.

The illustration given by the Restatement Second of Agency section 393 Comment e (1958) is a particularly instructive in this case:

> A is employed by P as manager for a year. Before the end of the year, A decides to go into business for himself; in anticipation of this and without P's knowledge he contracts with the best of P's employees to work for him at the end of the year. At the end of the year, A engages in a competing business and employs the persons with whom he has previously contracted. A has committed a breach of his duty of loyalty to P.

While authority can be found holding that many individual things can be done by an employee to engage in competition with a former employer, the engaging in more than isolated instances of such activity is what is prohibited. Here, when the numerous actions of defendants all aimed at obtaining the business of plaintiffs' Stockton facility for themselves are viewed together, they

constitute unfair competition and a breach of defendant Maashoff's fiduciary duty of loyalty to plaintiffs.

> We need not decide whether any of these acts would constitute a breach of fiduciary duty, taken alone, since there can be a little doubt that, in combination they show a course of conduct which falls demonstrably short of 'the most scrupulous observance' of an officer's duty to hi corporation. Bancroft-Whitney v. Glen, 64 C.2d 327

Defendant Maashoff was in a particularly advantageous position to undermine the business handled by plaintiffs' Stockton facility. He had been the manager of that facility and was in fact, if not in title the effective manager of the facility and representative of plaintiffs in Stockton for sixteen months immediately preceding the events triggering this action. Although he did not have the authority to hire and fire, he controlled the employees, he had access to the computer software, he had access to all of the records of the entire business of plaintiffs, including employees records. Defendants here have rolled all into one the things proscribed by the Restatement, by Klamath Orleans Lumber (1978) 87 C.A.3d 458, 151 C.R. 118, and by Bancroft-Whitney v. Glen, supra.

In 1983, the CPIS defendants sold to American Bankers Insurance Company a tracking system. There is no prohibition of such a sale of the underlying program alone. However, the system sold contained materials owned by plaintiffs. However, the system sold contained materials owned by plaintiffs. The CPIS defendants agreed to remove all such material. However, the tapes of the American Bankers program disclose significant

amounts of plaintiffs' material. Further, there is sufficient evidence that defendants are using plaintiffs' programs and materials in the operation of the Trans Global Stockton Service Center tracking system.

The defendants' case is further hindered in that Martin Atherton did not preserve the prior March of 1981 base program, or a tape of it.

Plaintiffs' Exhibit 28 (A, B, and C) is a comparison of thirty sections of program coding from Balboa, American Bankers and Trans Global. Exhibit 28 (A, B and C) is a clear example of where modifications and "fixes" were made to Balboa programs after March of 1981 and paid for by Balboa, but were left in the American Bankers program when sold by defendants and used by the defendants' Trans Global competing system. This is verified by the testimony of the court-appointed expert, Larry A. Dold.

Defendants' Affirmative Defenses

Defendants have the burden of proving their affirmative defenses. Evidence Code §500.

The affirmative defense that the complaint fails to state a cause of action has no validity.

The affirmative defense that the contracts contained in Exhibits 1(a) through 1(d) are against public policy as an invalid covenant not to compete which is in restraint of trade has no validity as a matter of law. This contention was rejected by the Court in denying defendants' Code of Civil Procedure section 631.8 motion for judgement. The Court deems the language of the covenant contained in

plaintiffs' Exhibit 1(d) to be an express covenant not to interfere or in any manner jeopardize the insurance accounts that had been assigned to Balboa in satisfaction of the $702,000 indebtedness of CPI. Breach of that covenant, through the soliciting away of the accounts, constitutes one of the elements of unfair competition claimed by plaintiffs.

The affirmative defense that the non-competition clause expired by its own terms has no validity, first because there is no non-competition clause in Exhibit 1(d), and second because the six month limitation contained in Exhibit 1(c), pertaining to defendant Nelson as an individual guarantor, does not nullify the provision in Exhibit 1(d) whereby the corporate defendants agreed to take no action whatsoever to cause the assigned policies of insurance to be cancelled, lapse or otherwise terminate, there being no time limitation on such express covenant.

Damages

It is generally recognized that loss of profits is the proper measure of damages for the misappropriation of trade secrets (Annotation, 11 ALR 4th 12), as well as for other forms of unfair competition (see, for instance, recent Michigan decision of Hayes-Albion v. Kuberski (Mich. 1981) 311 N.W.2d 122).

In Klamath-Orleans Lumber v. Miller, 87 C.A.3d 458, an unfair competition action where confidential customer lists were used by former employees to divert business from plaintiff, a manufacturer of devices to bind loads on trucks, the damages awarded to plaintiff constituted the profits from the sales diverted by defendant from plaintiff through the use of such confidential lists.

In Southern California Disinfecting Company v. Lomkin, 183 C.A.2d 431, the damages awarded for the soliciting away of plaintiff's customers by a former employee was the loss of prospective profits from the business that was solicited away, based upon the test of "reasonable probabilities."

Plaintiffs offered the testimony of Alex Majzoub, an insurance analyst in the collateral protection department of Balboa, on the issue of damages. Based on the closing of Balboa's Stockton Service Center and the transferring of Balboa's accounts by defendants, Balboa sustained damages for loss of profits. Loss of profits has two components, underwriting income and investment income. Testimony was produced that over a 25 year period, plaintiffs' loss of profits would be $3,721,000 (plaintiffs' Exhibit 25). Exhibit 25 summarized Mr. Majzoub's projection of lost profits from five groups of accounts, those of Trans Global, CFIA, CFIA of Nevada, Sutherland and Exhibit A, all of which were on the Stockton system in April, 1984 and were taken by defendants to the Trans Global system. The projection was based upon the history of premium income generated and profit realized from those accounts for calendar 1981, 1982 and 1983.

Exhibit 25, although recognizing loss of accounts over time, makes no provision for reducing to present value the cumulative total of plaintiffs' loss. Defendants presented no evidence from which the Court might discount the total to present value. The dollar amount of premium written and of profit from any given account tends to increase over time, in part, at least, as the value of the loan collateral being tracked increases with growth of the lender's business as well as with inflation. The evidence was uncontradicted that the Stockton tracking system

experienced dramatic growth during the three years plaintiffs operated it. The net written premium of the Exhibit A accounts alone grew by 40% from 1982 to 1983, and from 1981 to 1983 had increased by a factor of 3.37. Considering all of these circumstances, the Court believes the sum of $3,721,000 as presented in exhibit 25, which projects no growth within any of the accounts on the Stockton system, is as fair an approximation of present value of the loss suffered by plaintiffs as can be determined at this time, in effect offsetting future growth against discount to present value, both of which attempt to anticipate future events and are similarly speculative.

The "out-of-pocket" moving cost was not sufficiently documented for the Court to award such an amount to plaintiffs.

Defendants sold licenses to the tracking system containing plaintiffs' enhancements for $300,000. Plaintiffs are entitled to one-half of said sum, or $150,000.

Recapitulation

Loss of profits	$3,721,000
Profits from sale of software	150,000
Total award to plaintiffs	$3,871,000

Punitive Damages

Although the prayer of the complaint contains a request for punitive damages, there are no charging allegations in the body of the complaint to justify such an award.

Assuming the Court could render an award of punitive damages, the Court finds that such an award is not warranted in this case. The Court finds insufficient evidence of actual malice with the intention to vex, harass, annoy or injure plaintiffs.

Injunctive Relief

Despite the fact that the complaint is entitled "Complaint for Injunction and Damages," and contains adequate allegations justifying injunctive relief, the prayer, apparently through oversight, asked for an injunction only as a temporary restraining order.

Since a preliminary injunction has been issued in this case, the Court probably has authority under the "such other and further relief as is meet and proper" part of the prayer to grant a permanent injunction if otherwise warranted.

Plaintiffs are not asking for a permanent injunction, but only "a temporary total ban on use of the system for a periods that gained unfairly by the defendants." Plaintiffs suggest that the Court permit resumptive use of the tracking system after an initial limited total ban, upon payment of an appropriate licensing fee of 40% of the tracking income for three year and then 10% for the next

five years. Plaintiffs have cited no authority for imposing such condition (as payment of a licensing fee).

It is the decision of the Court that a permanent injunction not be granted in this case, as to do so would create a myriad of law suits or contempt proceedings and a hearing or trial again to determine the issue of plaintiffs' enhancements or modifications in defendants' support system. The Court deems the award of damages sufficient compensation for plaintiffs.

Attorneys Fees

Under California law, attorneys fees are not recoverable in unfair competition actions which have been brought outside of the Unfair Practices Act (Business and Professions Code sections 17000-17101). (Dachmayr Gunworks v. Olin Mathieson Chemical Corp. (9th Cir., 1974) 502 F.2d 802, 809-812.)

Accordingly, none is awarded herein.

Defendants Who Are Liable

There were originally thirteen defendants named in the complaint. At trial, counsel appeared for all defendants, including the "Trans Global" defendants, explaining in his opening statement that "Trans Global Insurance Company" has several divisions which engage in various other businesses: real estate, aviation and more recently collateral insurance tracking. No distinction was made among the various Trans Global entities by counsel or the witnesses, including those owning or employed by Trans Global, all referring simply to "Trans Global." It is evident that Trans Global is a single enterprise which

operates in various guises and which participated in the event of which plaintiffs complain in several of its various embodiments. The related Trans Global entities appeared by counsel and participated in the trial as simply "Trans Global." Transfer of corporate stock during the course of litigation does not affect the position of the corporation in the litigation. Thus the judgement should run against all manifestations of the Trans Global enterprise, including Trans Global Equities, Inc.

Defendants' Code of Civil Procedure section 998 offer as to Linda Maashoff was accepted by plaintiffs or defendants' motion for judgement pursuant to Code of Civil Procedure section 631.8 was granted. Defendants' Code of Civil Procedure section 631.8 motion for judgement was also granted as to defendants Patricia Hoelle, Charlene Nelson and John Nelson. The Court finds that there is insufficient evidence to impose personal liability upon the individual defendants Don Hoelle, Richard H. Klein, Woodburn Gailey and Barry Maashoff. Accordingly, plaintiffs take nothing against those defendants, with each party to bear his own costs.

The corporate defendants acted in concert to compete unfairly with plaintiffs, both with respect to the soliciting away of accounts and in establishing the competing Trans Global center. Trans Global, as Trans Global Insurance Services, Inc. and Collateral Protection Insurance Services formed a joint venture known as Trans Global Financial Service Center, Inc. to establish the competing Trans Global tracking center. Defendants John Nelson and Barry Maashoff testified they acted at all times as officers and agents of their respective corporate entities; consequently, since they participated in doing the acts of unfair competition, their respective corporate entities

participated in those acts of unfair competition. Collateral Protection Insurance Services, Consolidated Financial Insurance Agency of Nevada and the Trans Global enterprise including its many manifestations all participated in the acts of unfair competition found herein.

It is the decision of the Court that the plaintiffs take judgement against the corporate defendants Collateral Protection Insurance Services, Consolidated Financial Insurance Agency and Consolidated Financial Insurance Agency of Nevada, as well as Trans Global in whatever form or name it may exist, including Trans Global Insurance, Trans Global Insurance, Inc., Trans Global Insurance Company Inc., Trans Global Insurance Corporation, Trans Global Insurance Corporation, Inc., Trans Global Equities, Trans Global Equities, Inc., Trans Global Insurance Services, Trans Global Insurance Services, Inc., Trans Global Financial Insurance Services, Trans Global Financial Insurance Services, Inc., Trans Global Insurance Agency, Trans Global Insurance Agency, Inc., Trans Global Financial Service Center and trans Global Financial Service Center, Inc.

Let judgement be entered accordingly.

Dated: 7-18-86

s/ Frank Kim
FRANK KIM
JUDGE OF THE SUPERIOR COURT

SUPERIOR COURT OF CALIFORNIA

COUNTY OF SAN JOAQUIN

BALBOA INSURANCE COMPANY, et al.,

Plaintiffs,

v.

TRANS GLOBAL EQUITIES, et al.,

Defendants.

No. 176696

JUDGEMENT

Filed July 22, 1986

After trial to the Court sitting without a jury, Darrell Glahn and Donald West appearing for plaintiffs and George Corey of Corey, Orton, Luzaich & Gemello and Velma Lim of Kroloff, Belcher, Smart, Perry & Christopherson appearing for defendants, IT IS ORDERED:

1. Plaintiffs take nothing from defendants Linda Maashoff, Patricia Hoelle, Charlene Nelson, John Nelson, Don Hoelle, Richard H. Klein, Woodburn Gailey and Barry Maashoff, each party to bear his own costs;

2. Plaintiffs have and recover from defendants Collateral Protection Insurance Services, Consolidated Financial Insurance Agency and Consolidated Financial

Insurance Agency of Nevada, as well as Trans global in whatever form or name it may exist, except Trans Global Equities, Inc., including Trans Global Insurance, Trans Global Insurance, Inc., Trans Global Insurance Company, Trans Global Insurance Company, Inc., Trans Global Insurance Corporation, Trans Global Insurance Corporation, Inc., Trans Global Equities, Trans Global Insurance Services, Trans Global Insurance Services, Inc., Trans Global Financial Insurance Services, Trans Global Financial Insurance Services, Inc., Trans Global Insurance Agency, Trans Global Insurance Agency, Inc., Trans Global Financial Service Center and Trans Global Financial Service Center, Inc., Three Million, Seven Hundred and Ninety-Six Thousand Dollars ($3,796,000.00) together with costs in the further sum of $

3. From Collateral Protection Insurance Services, Consolidated Financial Insurance Agency and Consolidated Financial Insurance Agency of Nevada the further sum of Seventy-Five Thousand Dollars ($75,000.00).

4. Notice having been received that Trans Global Equities, Inc. has filed for protection under Chapter 11 of the Federal Bankruptcy Act, case number 38601924 JR in the Northern District of California Bankruptcy Court, the Court severs the claims of plaintiffs against Trans Global Equities, Inc. and no judgement is at this time being

rendered against Trans Global Equities, Inc., the court reserving jurisdiction with respect to Trans Global Equities, Inc. herein.

Dated:7-22-86

s/ FRANK KIM
FRANK KIM
JUDGE OF THE SUPERIOR COURT

Supreme Court, U.S.
FILED
OCT 1 1990
JOSEPH F. SPANIOL, JR.
CLERK

(2)

No. 90-407

In The

Supreme Court of the United States

October Term, 1990

COLLATERAL PROTECTION INSURANCE SERVICES, CONSOLIDATED FINANCIAL INSURANCE AGENCY, CONSOLIDATED FINANCIAL INSURANCE AGENCY OF NEVADA, AND BARRY MAASHOFF,

Petitioners,

v.

BALBOA INSURANCE COMPANY, NEWPORT INSURANCE COMPANY, NEW PORT MANAGEMENT CORPORATION, AND INSURANCE AUTOMATION CORPORATION,

Respondents.

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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RESTATEMENT OF QUESTION PRESENTED

The facts do not present the issue petitioners suggest. The judgment below did not award damages for the reproduction of computer software. Neither did that judgment protect against copying of trade secrets. The judgment below awarded $3,721,000 in damages for loss of insurance underwriting and investment profits caused by the taking of respondents' business by petitioners' unfair acts in violation of state law. In addition to that unfair competition recovery, respondents were awarded $150,000 for the sale by petitioners of computer software owned by respondents. Thus, the question is:

Does this Court have jurisdiction to review the judgment of the state court awarding damages for loss of insurance underwriting and investment profits in the amount of $3,721,000 for unfair conduct of petitioners in violation of state law because, in addition to that unfair conduct, petitioners also misappropriated respondents' computer software, for which respondents were awarded the additional sum of $150,000 and if it does, should it?

PARTIES RESPONDENT

Balboa Insurance Company

Newport Insurance Company

Newport Management Corporation

Insurance Automation Corporation

PARENT AND SUBSIDIARY CORPORATIONS

Textron, Inc.

AVCO Financial Services, Inc.

AVCO Financial Services International, Inc.

Balboa Life Insurance Company

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BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

Facts

Petitioners' statement of the facts of this case is incomplete and misleading, as demonstrated by the following from the opinion of the Court of Appeal but omitted in petitioners' statement of the "factual background" of the case:

1. While managing Balboa's tracking center in late 1983, Barry Maashoff began preparing to open the competing Trans Global insurance tracking service. (Petitioners' Appendix, 7a)

2. While still the managing agent for Balboa, Maashoff became manager of the Trans Global center and began planning for the new center's building and equipment in January of 1984. (PA 8a)

3. While still acting as agent of Balboa, for which he was being paid $1,500.00 per month, Maashoff planned the personnel requirements for defendants' competing center. (PA 8a, 39a)

4. Maashoff evaluated plaintiffs' personnel with Jan Melhaff, a department supervisor in plaintiffs' Stockton service center, to determine which of them to recruit for Trans Global. (PA 8a, 46a)

5. At the same time Maashoff began planning to move accounts from Balboa to Trans Global. (PA 8a)

6. Petitioners had a telephone line installed in Balboa's office to route calls directly from the Balboa service center to Trans Global's new center. (PA 9a)

7. Petitioners arranged for underwriting of collateral insurance with another carrier. (PA 9a)

8. For petitioners' new center, Maashoff recruited department supervisors Jan Melhaff and Darrell Fenley, as well as employee Jodi Thomas and advised other Balboa employees of the availability of jobs with Trans Global. (PA 9a)

9. Petitioners kept all of these activities secret from Balboa. (PA 8a & 46a)

10. In early May, Maashoff had Susan McCrory, a computer programmer for Balboa in Stockton, bring to Trans Global programs she had been working on for Balboa and spend her two week vacation working on them for Trans Global. (PA 10a, 43a)

11. Petitioners solicited the accounts previously sold to Balboa to leave Balboa and come to the Trans Global tracking center. (PA 9a)

12. Petitioners promised lenders there would be no change occasioned by the transfer, that the personnel and even the mail box would remain the same as would the procedures and tracking system. (PA 9a, 45a)

13. Barry Maashoff attempted "to solidify a loyal base of employees for Trans Global" with Balboa's employees at the Stockton service center. (PA 9a, 46a)

14. Maashoff tried to induce Darrell Fenley to organize a walkout to paralyze Balboa's Stockton tracking service operation. (PA 10a)

15. Petitioners told Balboa's tracking service clients of Balboa's lender account tapes and urged them to demand the information on them from Balboa. (PA 10a)

16. Petitioners had Balboa's Stockton employees delay notifying Balboa in Irvine when clients requested a move to Trans Global, while yet forwarding the client information tapes directly to Trans Global. (PA 10a)

The viability of Trans Global's new tracking center depended on the ability of defendants to offer Balboa's clients a complete service package duplicating as much as possible the procedures and personnel of Balboa's Stockton tracking center. (PA 45a) The critical factor in this endeavor was Barry Maashoff. (Petitioner's Appendix p. 46a) In establishing the competing center, Barry Maashoff, as the actor for the remaining defendants, breached his duties of confidentiality and loyalty to Balboa by setting up the competing tracking center and luring Balboa's clients and employees away. (PA 44a) For these acts causing Balboa's loss of insurance business income, the trial court awarded $3,721,000. (PA 75a)

REASONS THE WRIT SHOULD BE DENIED

I. This Case Does Not Present The Question Petitioners Pose

The facts in the record do not raise the question presented by petitioners. The judgment below did not award "damages under state law for the reproduction of computer software", except incidentally. Damages were awarded primarily for petitioners' acts of unfair competition in violation of state law having nothing to do with reproduction of computer software. The state law applied below was not "to protect against copying of trade secrets", but to protect against petitioners' taking of respondents' insurance business by unfair business practices in violation of state law which incidentally included misappropriation of respondents' software modifications. (PA 74a, 75a)

A. The judgment below was for violation of state law.

17 U.S.C. §301 provides:

> (b) Nothing in this title annuls or limits any rights or remedies under the common law or statutes of any State with respect to . . .
>
> (3) activities violating legal or equitable rights that are not equivalent to any of the exclusive rights within the general scope of copyright as specified by §106.

Since §301(b)(3) preserves to the states all rights except those falling within the general scope of copyright as specified in §106, the initial inquiry is whether copyright is at all involved.

There was no claim in the trial court either of copyright infringement or of preemption. (PA 13a) The case made out in the trial court was identical in principle with *Bancroft-Whitney v. Glen*, 64 C.2d 327, 49 C.R. 825 (1966), a case arising long before the advent of computer software and involving no question of copyright. Merely listing the facts common to both *Bancroft-Whitney* and this case makes this clear:

1. the action was based on breach of fiduciary duty;

2. the complained acts took place during employment;

3. the employer sought no restrictions on the use of skills and knowledge gained while employed;

4. no publicly marketed product disclosed plaintiff's confidential information;

5. a cream of the crop recruitment list was created;

6. fellow employees were solicited;

7. a competitive business was formed;

8. all actions were done in secret;

9. the competitive business was aware of and ratified the actions;

10. the only source of experienced staff for the competitive business was from the plaintiff; and

11. trade secret was established. (In the case on petition, the computer software was but one of several trade secrets, including the support system for the clients, the commission structure of Balboa's agents, information concerning Balboa's employees and other information concerning clients and accounts.) (PA 21a)

Also compelling and unrelated to copyright is Comment E to Section 393 of the *Restatement of Agency*, quoted in the opinion of the California Court of Appeal: (PA 47a)

> A is employed by P as manager for a year. Before the end of the year, A decides to go into business for himself; in anticipation of this and without P's knowledge he contracts with the best of P's employees to work for him at the end of the year. At the end of the year, A engages in a competing business and employs the persons with whom he was previously contracted. A has committed a breach of his duty of loyalty to P.

The names of the parties here could be inserted without necessitating any change in the Comment.

Since the question of copyright preemption was raised initially on appeal, there is no record on any copyright issue, including the claim of preemption, in the trial court. (PA 13a) As the California Court of Appeal noted at footnote 16 (PA 16a), the record provides no basis for determining applicability of copyright protection here.

B. The award of $3,721,000 was not for violation of any right protected by §106.

Section 106 protects the rights of an owner of a copyrighted work to produce, distribute, perform and display the work exclusively. (Petition p.3) None of the things for which respondents recovered the sum of $3,721,000 included any of these things. (PA 75a) Neither the acts on which liability rested as shown by the facts from the California Court of Appeal opinion outlined at page 1 above, nor the interests protected, including respondents' loss of insurance underwriting and investment income, in any way resemble reproduction, distribution, performance or display of a copyrighted work or anything "equivalent".

Petitioners argue that the software was the key ingredient necessary for the success of their plot. Even were this true, it would not convert their acts of unfair competition in violation of state law into violations of copyright or rights equivalent to rights of copyright protected by §106.

The statute covers certain enumerated rights and their equivalents. Petitioners ask this Court to extend the sweep of the statute to things which by the very terms of

their petition can be seen to be far beyond its scope. There is no logical limit to the "House that Jack Built" argument petitioners advance. According to that argument, anything which may be affected by a right protected by the Copyright Act falls within its purview. Apparently hiring away respondents' key employees in violation of fiduciary duty is "copying" within the scope of the act, so that state law may not prohibit it. In essence, petitioners urge that so long as the miscreant can point to some relationship to another wrongful act which may violate a right of copyright, the states are powerless to redress the wrongful conduct.

Contrary to petitioners' rather convoluted argument that the California Court of Appeal's decision opens the way for a reversal, (Petition p.8) the Court of Appeal expressly decided on grounds other than trade secret in affirming the judgment:

> We need not determine, however, whether the lists and identities here technically were trade secrets. In this case, the sum of the actions speak louder than any of the individual parts. Rather, we shall conclude that Maashoff breached his duty of fidelity and confidentiality to Balboa by setting up a competing Business and luring Balboa's clients and employees away unfairly. (PA 44a)

Therefore, even were petitioners to prevail on the preemption argument with respect to copying, the judgment, except possibly to the extent of the $150,000 for sale of the software, will remain intact in favor of respondents for $3,721,000.

C. The award of additional damages for sale of the software was independent of the award for $3,721,000 for loss of insurance business profits.

The sale of the software to American Bankers was separate from the scheme to take respondents' business. The sale to American Bankers was in early 1983 (PA 7a), while the scheme of unfair competition developed in late 1983 and unfolded in 1984. (PA 7a-10a)

D. Petitioners' attack does not reach the substance of the judgment.

Petitioners focus on one discrete, minuscule aspect of the case as a basis for review, claiming their misappropriation of Balboa's software modification invokes federal preemption. The question petitioners raise relates to only 3.875% of the award. As the Court of Appeal pointed out below, even in the misappropriation area which it found to be preempted, only such of the remedy is preempted as relates to material which might properly be copyrightable. Otherwise, any claim for misappropriation survives. (PA p.38a & §301(b)(3)) Thus, even were petitioners to prevail in this Court, it would result in an insignificant modification of the judgment, since it is clear from an examination of the facts that the judgment for $3,721,000 rests on rights separate from the software misappropriation. As noted previously, the California Court of Appeal rested its decision expressly on grounds other than misappropriation of the software. (PA 44a)

II. The Conflict And Confusion Claimed By Petitioners As Reason For Granting The Writ Do Not Exist.

Even when applying the "subjective" extra element test, the courts make a clear differentiation between cases which involve rights in the nature of rights of copyright and those which involve rights which are not classic rights of copyright. The difference in result which petitioners attribute to a difference in approach by the courts is dictated instead by the nature of the right at issue in each case. Where that right is purely in the nature of classic or historic copyright, there is preemption; where there are rights under state law which are not those of classic copyright, the state action is not preempted. This is the analysis of Professor Nimmer, *Nimmer on Copyright* (1963, 1990 Rev.) §1.01[B] pp.1-11 *et seq.* and examination of the cases discussed by petitioners in §I B (Petition p.14) reaffirms its validity:

Avco Corp. v. Precision Air Parts, Inc., 210 U.S.P.Q. (BNA) 894 (M.D. Ala. 1980), aff'd on other grounds, 676 F.2d 494 (11th Cir. 1982)	Copying, but preemption issue not reached by appellate court.
Brignoli v. Balch Hardy and Scheinman, Inc., 645 F.Supp. 1201 (S.D.N.Y. 1986)	Seven non-copyright causes of action including trade secret and breach of confidentiality. No preemption.
M. Bryce & Assoc. v. Gladstone, 319 N.W.2d 907 (Wis.App. 1982)	Trade secret involved simply not equivalent to copyright at all. No Preemption.

Crow v. Wainwright, 720 F.2d 1224 (11th Cir. 1983)	Copying and distribution. Preemption.
Del Madera Properties v. Rhodes and Gardner, Inc., 820 F.2d 973 (9th Cir. 1987)	On court's analysis, nothing added to copying and distribution; no extra element. Preemption.
Ehat v. Tanner, 780 F.2d 876 (10th Cir. 1985)	Copying and publishing. Preemption.
Gladstone v. Hillel, 203 C.A.3d 977, 250 C.R. 372 (1988)	Conversion of jewelry and molds. No preemption.
Harper & Row Publishers, Inc. v. Nation Enterprises, 723 F.2d 195, (2d Cir. 1983), rev'd on other grounds, 471 U.S. 539 (1985)	Copying and distribution. Preemption.
Robert H. Jacobs v. Westoaks Realtors, Inc., 159 C.A.3d 637, 205 C.R. 620 (1984)	Distribution. Preemption.
Maheu v. CBS, Inc., 201 C.A.3d 662, 247 C.R. 304 (1988)	Interference with contract based solely on copying and publication. Preemption.
Mayer v. Josiah Wedgewood & Sons, Ltd., 601 F.Supp. 1523 (S.D.N.Y. 1985)	Copying and distribution. Preemption.
Motown Record Corp. v. George A. Hormel & Co., 657 F.Supp. 1236 (C.D.Cal. 1987)	Copying and distribution. Preemption.
Oddo v. Ries, 743 F.2d 630 (9th Cir. 1984)	Breach of fiduciary duty plus copying. No preemption.

Peckarsky v. American Broadcasting Co., Inc., 603 F.Supp. 688 (D.D.C. 1984)	Both copyright and non-copyright. Non-copyright contract issues not pre-empted.
P.I.T.S. Films v. Laconis, 588 F.Supp. 1383 (E.D.Mich. 1984)	Breach of fiduciary duty. No preemption.
Rand McNally & Co. v. Fleet Management Systems, 591 F.Supp. 688 (N.E.Ill. 1983)	Breach of fiduciary duty. No preemption.
Ronald Litoff, Ltd. v. American Express Co., 621 F.Supp. 981 (S.D.N.Y. 1985)	Both copyright and non-copyright. Non-copyright claims not preempted.
Schuchart & Assoc., etc. v. Solo Serve Corp., 540 F.Supp. 928 (W.D.Tex. 1982)	Breach of contract. No pre-emption.
S.O.S., Inc. v. Payday, Inc., 886 F.2d 1081 (9th Cir. 1989)	Trade secret action, Cal. Civ. Code §3426 *et seq.* Not preempted.
Videotronics, Inc. v. Bend Electronics, 564 F.Supp. 1471 (D.Nev. 1983)	Copyright only. Preemption. No factual basis for discussion of trade secret; pure *dicta*.
Warrington Asso[illegible] v. Real-Time Engineering Systems, 522 F.Supp. 367 (N.D.Ill. 1981)	Trade secret distinguished from copyright. No pre-emption.
Whelan Associates, Inc. v. Jaslow Dental Laboratory, 609 F.Supp. 1307 (E.D.Pa. 1985), aff'd 797 F.2d 1222 (3d Cir. 1986), cert. denied sub nom. *Jaslow Dental Laboratory, Inc. v. Whelan Associates, Inc.*, 479 U.S. 1031 (1987)	Copying, preparation of derivative work and sale. Preemption.

Some of petitioners' confusion may stem from basing their analysis on the claims of plaintiffs rather than on the findings of the courts. Preemption depends on what the courts found, rather than what the parties claimed.

The courts in each of these cases clearly delineated the elements which controlled the outcome. There was no confusion. The approach taken in each opinion was dictated by the facts. Where purely classic copyright issues were alone present, they were the focus of the opinion. Where issues of state law were present, they were the focus and where the state law presented issues different from copyright, state law was not preempted. Both the principle and the application appear clear.

From even a cursory examination of the cases cited it is evident there is no confusion in the cases, only in petitioners' analysis.

Petitioners' analysis that "Courts that focus on the act of copying universally hold the state law preempted" (Petition p.17) is suspect, since *Rand McNally, Pecharsky* and *Gladstone,* all cited for this proposition, (Petition p.18) found claims for breach of fiduciary duty, contract breach and conversion were *not* preempted.

While petitioners may wish the opinion in *Aloha Airlines Inc. v. Director of Taxation,* 464 U.S. 7 (1983), had used different language, the case was decided in the context of taxation of interstate commerce and the language of the opinion was much more specific and less helpful to petitioners than the paraphrase offered as a quotation. (Petition p.13)

CONCLUSION

Although petitioners have attempted to craft in words an issue which might meet the standards for review by this Court, the facts of the case do not support the statement of the issue or the existence of any basis on which the issue as stated can be reviewed. The statement in the conclusion of petitioners' argument (Petition p.21) that "[i]f the application of the remedy is triggered by the act of copying, that remedy is equivalent to copyright and therefore preempted," points up the deficiency of the petition. The facts, such as the hiring away of respondents' employees, are clear that the application of the state remedy was not "triggered" by the act of copying the software. That failing, even on petitioners' statement of their position, there is no basis for review and the writ should be denied.

Respectfully submitted,

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